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March 1991 (First of Two March Issues)

LETTING THE STUDENTS PAY

Introduction: The state budget pressures are affecting higher education in ways that may produce major changes in student opportunities and the roles of public institutions.

The Budget Problem Grows: Compilations by the National Conference of State Legislatures (NCSL), State Budget & Tax News, and the National Governors' Association (NGA) show about 30 states are experiencing shortfalls in their current (FY 1991) general fund budgets. Because this list includes nearly all of the largest states and excludes primarily smaller Western states, about 80% of U.S. population lives in states with shortfalls. States with imbalance in their new (FY 1992) budgets are harder to count because of differing definitions of baseline budgets. The number is somewhere near the 34 recently counted by State Budget & Tax News. Many states have been revising their revenue estimates downward in the last month, making the current situation worse than indicated by any of these surveys.

Higher Education As A Target For Cuts: "Not since the early 1980s has higher education been in such dire financial straits," according to the Chronicle Of Higher Education (2/27). With isolated exceptions, higher education hasn't been singled out as a target for budget cutting. Budget cutters aren't saying more money is unnecessary, just that they can't afford to provide it. While not necessarily a per se target for cuts, higher education is frequently reached by the process of elimination. So, its cuts are often disproportionate to those for other categories of state spending.

Increases in welfare are linked to increasing caseloads and to policies in most states not to cut payment levels to welfare families. Medicaid increases of 15% or more in many states are driven by the welfare caseload, federal mandates, and increasing health costs. Corrections costs are being driven by prisoner count increases. Elementary and secondary education is being protected economically by property taxpayers, who might have to pay if the state doesn't, strong teacher organizations, and substantial commitment by state elected officials. Thinking along these lines has concentrated the cuts in FY 1991 and especially FY 1992 on functions such as local aid other than schools, state operations, and higher education.

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Cuts in higher education also tend to be attractive, at least relative to other cut options, because they offer the best of both worlds. They appeal to those who believe spending is too high in universities. But they also can appeal to those who don't favor cuts, but believe tuition can be raised to combine reasonable spending levels with stable or even declining state appropriations.

State Higher Education Appropriations: The states have developed quite divergent levels of support as indicated by the appropriations per student (excluding capital outlays) shown in Table 1.

Table 1: Higher Education Appropriations Per Student, FY 1990

Rank	State	Amount	Pct. Av.	Rank	State	Amount	Pct. Av.
1	Alaska	\$10,084	230%	26	Oregon	\$4,105	94%
2	Hawaii	8,092	184	27	Illinois	4,099	93
3	New York	6,108	139	28	Virginia	4,089	93
4	Connecticut	6,071	138	29	Michigan	4,086	93
5	New Jersey	5,944	135	30	Arizona	4,085	93
6	Wyoming	5,942	135	31	Oklahoma	4,074	93
7	Florida	5,673	129	32	Indiana	4,044	92
8	Maine	5,311	121	33	South Carolina	4,038	92
9	Massachusetts	5,142	117	34	Kansas	3,954	90
10	California	5,099	116	35	Missouri	3,661	83
11	Washington	4,697	107	36	Nebraska	3,586	82
12	New Mexico	4,695	107	37	Ohio	3,577	82
13	Nevada	4,601	105	38	Kentucky	3,552	81
14	Delaware	4,594	105	39	Montana	3,542	81
15	Minnesota	4,571	104	40	Arkansas	3,486	79
16	Idaho	4,518	103	41	Alabama	3,467	79
17	Maryland	4,476	102	42	South Dakota	3,348	76
18	Rhode Island	4,475	102	43	Texas	3,341	76
19	Iowa	4,445	101	44	North Dakota	3,137	72
20	Georgia	4,442	101	45	Mississippi	3,018	68
21	Wisconsin	4,411	101	46	Colorado	2,927	67
	United States	4,388	100	47	Louisiana	2,854	65
22	North Carolina	4,318	98	48	New Hampshire	2,677	61
23	Utah	4,293	98	49	West Virginia	2,592	59
24	Tennessee	4,150	95	50	Vermont	2,421	55
25	Pennsylvania	4,147	95				

Spending well above average is found in Alaska, Hawaii, and Wyoming -- consistent with their extraordinarily good fiscal positions. The other states that exceed the national average by 10% or more enjoyed more than average prosperity in the late 1980s, but now have some of the worst fiscal problems in the nation -- California, Connecticut, Florida, Maine, Massachusetts, New Jersey, and New York. The battle over higher education funding is likely to be most heated

in those states. Because of their fiscal circumstances, the outcome may be least satisfactory for higher education interests.

State And Student Funding: A recent NCSL survey of legislative leaders (Leaders' Outlook: 1991) suggested:

The pattern for higher education funding has been to decrease the state share and increase the institutional share. Where this trend continues, the relationship between the universities and the legislature undoubtedly will be tense.

The percentage of operating costs defrayed by tuition is shown in Table 2.

Table 2: Percentage Of Operating Cost Paid By Tuition, FY 1990

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	Hawaii	7.9%	18	Montana	23.0%	34	Wisconsin	30.4%
2	California	8.5	19	Connecticut	23.2	35	Mississippi	30.8
3	Wyoming	11.9	20	New Jersey	23.2	36	Virginia	31.2
4	Alaska	12.4	21	Oklahoma	23.5	37	Iowa	31.3
5	Idaho	13.2	22	Massachusetts	24.0	38	Indiana	32.1
6	New Mexico	14.8		United States	24.1	39	South Dakota	32.2
7	North Carolina	15.3	23	Nebraska	24.8	40	Rhode Island	32.7
8	New York	16.9	24	Kansas	25.6	41	North Dakota	34.7
9	Florida	17.4	25	Maine	25.7	42	West Virginia	34.7
10	Washington	19.5	26	Tennessee	25.7	43	Ohio	37.7
11	Nevada	20.0	27	Oregon	25.8	44	Michigan	38.7
12	Illinois	20.2	28	Kentucky	26.7	45	Louisiana	39.3
13	Arizona	21.4	29	South Carolina	27.8	46	Pennsylvania	39.6
14	Georgia	21.8	30	Arkansas	28.2	47	Colorado	42.1
15	Texas	21.8	31	Missouri	29.2	48	Delaware	47.0
16	Utah	22.6	32	Alabama	29.5	49	New Hampshire	53.3
17	Minnesota	22.9	33	Maryland	29.7	50	Vermont	70.6

The standard range of state policy is for students to pay 20-40% of higher education costs. Only four smaller states -- Colorado, Delaware, New Hampshire, and Vermont -- exceed this level. Eight states are below it in the range of 10-20% while Hawaii and California were below 10% in FY 1990. Big changes are taking place in California (8.5%) and New York (16.9%) that will lift their percentages substantially and, because of their size, also lift the national average substantially. As a result of the state fiscal problems, FY 1991 and FY 1992 tuition changes are likely to exceed both: (1) inflation and (2) the increase in state appropriations per student.

In Missouri, for example, the Board of Curators had already approved a 6% increase in tuition, but didn't anticipate the governor's

budget. To avoid a tax increase in the face of poor revenue performance, it recommended a slight cut in higher education appropriations. The University of Missouri president suggested shifting to a 12% tuition increase to adjust to the expected budget. To avoid a major tax increase, Florida's governor is seeking fee increases of 20% for in-state students and 25% for out-of-state students.

Scholarships: One of the rationales of having state-sponsored universities is affordability, which is probably the argument most citizens would think of if asked to explain why state government should be in the university business. As a result, many legislators have difficulty in accepting the concept of high tuition at state institutions. The acceptance is particularly low when considering New England vocational-technical schools, which are historically extensions of the public schools as grades 13 and 14, community colleges, and in dealing with low income students. This concern explains the recent popularity of guaranteeing to certain "at risk" elementary students the chance to go to college if they do well through high school.

Scholarships are partially an antidote to higher tuition and fees at universities, preserving access for those who qualify on the basis of need. As a result, it is customary for proposals for higher tuition to be accompanied by the assurance that access won't be limited because an offsetting expansion of scholarship assistance will take place.

Scholarships come in three forms. The first are those generated outside of state government, such as foundations, trusts, and the federal government. The second is scholarship money from individual schools. The third, which is of most immediate interest in considering offsets to tuition, is state-administered scholarship programs. A total of \$2.15 billion is being provided by these programs this academic year. The largest programs are in New York (\$439 million), Illinois (\$203 million), California (\$165 million), Pennsylvania (\$146 million), Texas (\$118 million), New Jersey (\$102 million), Ohio (\$80 million), Minnesota (\$78 million), Michigan (\$75 million), Massachusetts (\$72 million), and Florida (\$69 million). The data show differences in state funding policies clearly when put on a per capita basis as done in Table 3.

New York tops the list in scholarship assistance (Table 3), notwithstanding its low reliance on tuition (Table 2), and its high per-student appropriations (Table 1) -- all statistics combining to show one major reason why the state's spending and taxes are well above comparable states. The two states most reliant on tuition (Table 2) have sharply different approaches to scholarships. Vermont (2nd on Table 3) provides the second highest level in the nation, while New Hampshire retains its low tax state policy by both high tuition and low scholarships.

Table 3: Per Capita State Scholarship Aid, FY 1991

<u>Rank</u>	<u>State</u>	<u>Amount</u>	<u>Rank</u>	<u>State</u>	<u>Amount</u>	<u>Rank</u>	<u>State</u>	<u>Amount</u>
1	New York	\$24.3	17	Ohio	\$7.4	34	Tennessee	\$3.7
2	Vermont	19.8	18	Colorado	7.3	35	Georgia	3.5
3	Minnesota	17.7	19	West Virginia	7.2	36	Delaware	2.8
4	Illinois	17.7	20	Texas	6.9	37	Kansas	2.7
5	Iowa	14.4	21	Utah	6.6	38	North Dakota	2.3
6	New Jersey	13.2	22	South Carolina	5.5	39	Arkansas	2.2
7	Pennsylvania	12.2	23	California	5.5	40	Nebraska	1.4
8	Massachusetts	11.9	24	Florida	5.3	41	New Hampshire	1.3
9	Oklahoma	11.1	25	Kentucky	5.2	42	Louisiana	1.2
10	Connecticut	11.0	26	Alaska	4.7	43	Arizona	0.9
11	Rhode Island	10.6	27	Washington	4.5	44	South Dakota	0.8
12	Wisconsin	9.1	28	Maryland	4.4	45	Idaho	0.7
13	New Mexico	8.8	29	Missouri	4.2	46	Mississippi	0.7
14	North Carolina	8.8	30	Maine	4.1	47	Hawaii	0.5
	United States	8.6	31	Oregon	4.1	48	Wyoming	0.5
15	Indiana	8.5	32	Virginia	4.1	49	Montana	0.5
16	Michigan	8.0	33	Alabama	3.9	50	Nevada	0.3

Non-Need Scholarships: If the state's role is viewed as assuring a college opportunity for a particular student, a strong argument can be made that the state can buy that opportunity as well as make it by providing universities. Responding to this argument, some states provide scholarships to residents who wish to attend private colleges and universities. This looks like a voucher plan for elementary and secondary education, so the policy has opponents among those who want to conserve scarce state funds for public institutions and those who oppose what they see as aid to institutions some of which are affiliated with religion. There are also non-needs scholarships, such as those designed to entice outstanding graduates of a state's high schools to attend its universities. Some states have no program of either type. Others have quite small programs. Table 4 shows those states with non-need scholarship programs of \$1 million or more for undergraduates in FY 1991.

Table 4: State Non-Need Scholarships (\$ million), FY 1991

<u>State</u>	<u>Amount</u>	<u>State</u>	<u>Amount</u>	<u>State</u>	<u>Amount</u>
Florida	\$40.5	Virginia	\$16.9	New Jersey	\$5.8
Ohio	26.8	Georgia	16.3	Maryland	5.0
North Carolina	24.6	Missouri	10.1	New Mexico	4.0
New York	24.2	Colorado	9.8	Oklahoma	2.9
Illinois	18.3	Alabama	6.5		

The Fate Of Scholarship Programs: While there is sentiment for scholarship programs to rise consistent with tuition increases, this outcome isn't guaranteed in any state's budget process. One of the more interesting debates will likely occur in Massachusetts, where the governor has recommended that current scholarship programs be converted to loans. He is also suggesting that public university tuition rates be set on a graduated basis, varying with student financial capacity.

University Response to Budget Reductions: The pattern in many states has been for the flagship institution(s) to respond to apparently inevitable budget reductions by measures that permit maintenance of faculty salaries, research programs, and other indicators accepted by academics as signs of excellence. The key to this is reducing enrollment, which translates into making it harder for the state's high school graduates to attend the flagship(s). This phenomenon has been particularly noticeable in the Midwest, with Kansas and Minnesota examples.

The concept is likely to hit California this year. California has three tiers of higher education: (1) community colleges, (2) the California State University system, and (3) the University of California system. Facing a shortfall estimated at \$7-10 billion, the governor's budget provides UC nearly \$300 million less than its definition of needs. The governor suggested a 20% increase in student fees, but UC officials are talking about a 40% increase, on top of 10% this year. The result, \$2,500 a year, would leave UC a low-tuition university system by national standards, but with outrageous tuition by historical standards of a state which broke its no tuition policy recently and still prefers the word "fees" to "tuition" as a way of describing what students must pay to attend.

According to the chairman of the UC Board of Regents the "tragic budget" will have another effect:

We will not cut back on quality. We will cut back on quantity if we have to but not on quality. It is my position that if we have to cut back in faculty, we will cut back in students. We would rather have a reduction in quantity, not quality.

This effect would be achieved by making it harder to get in. Students would need better credentials as indicated by grade point averages and Scholastic Aptitude Test scores.

TAX POLICY AND BUSINESS CLIMATE

Introduction: The simplistic view of economic development and business taxes is that a state should *tax business as little as possible* in order to provide an attractive business climate. A broader,

but also simple, view is that states attract businesses by *keeping all taxes, not particularly business taxes, low*. By the second theory, Florida, Nevada, and New Hampshire have lots going for them. All have low tax burdens and spending levels. None of the three has a personal income tax. Nevada has no corporate income tax. New Hampshire has no sales tax.

But when additional state money is needed, the absence of broad-based taxes on individuals like a personal income tax draws attention to raising property taxes, with heavy impact on business, and business taxes. This year, all three states have major debates over tax policy. They are considering ways to tax business, like versions of value added taxes, that could draw attention in other states. In all three states, there is considerable support for higher taxes from the business community itself, though the support isn't necessarily for the most popular tax options.

Fiscal Circumstances: The three states have experienced extraordinary economic growth in the 1980s. Florida and Nevada have become popular as retirement communities and have profited from immigration among the increasing ranks of the affluent elderly. In Nevada, the gaming industry has done well, encouraging additional Las Vegas hotel construction that itself has created many jobs and put the city on the map as a convention destination. Florida's tourism remains popular. New Hampshire has been drawing population oriented toward the metropolitan Boston area. All three states have had considerable success, from a low base, in attracting high tech manufacturing.

But economic growth has its costs in increasing demand for public services. This is particularly apparent in the demand for new infrastructure, but also appears in expanding school enrollments. The revenue structures of the three states are slow in reaping the benefits of growth. Nevada's growth has made the gaming industry, the source of much of the state's revenue, a smaller proportion of total economic activity. Expansion of state-funded social services puts New Hampshire in a sharply expanding spending mode while traditional revenue sources, like excise taxes, aren't rapidly growing. Florida relies heavily on sales taxes that haven't been growing as rapidly as spending. The problem was recognized some years ago by an expansion of the sales tax to services, but when opposition appeared the governor and legislature repealed the extension and raised the tax rate.

Florida has a shortfall in the current service budget for FY 1992. Before and after election, Governor Chiles indicated an interest in "tax reform," but said the legislature should obtain public confidence in government before raising taxes. New Hampshire has suffered economic reversals worse than just about any other state in the U.S., giving it major budget shortfalls. Nevada doesn't have a shortfall, but is likely to experience one as soon as its nation-beating rate of economic growth slows, as it must.

Recommendations For Florida: Florida's Chamber of Commerce recently released an extensive report on tax structure that skirts endorsement of higher taxes. The report suggests, "A good business climate now is about more than simply low taxes." The report places heavy emphasis on public spending on infrastructure, education, and helping business start-ups. It discusses tax principles on a revenue-neutral basis. However, in the Florida environment, the recommendations will be considered as ways of increasing total state taxes. Indeed, one of the indictments of the current system is a "growing awareness that Florida's fiscal foundation is inadequate for supporting state needs and fostering a stable business environment."

The report offers five options for reform. The first would expand the sales tax to goods currently exempt, but exempt business purchases of machinery and equipment. Property taxes would be reformed by assessment at full value and elimination of homestead exemptions. The second option would extend the sales tax to services excepting intermediate services provided to businesses whose final products will themselves be taxed. The third option is a single business (value added) tax to replace the corporate income tax and certain other business taxes. The fourth option is a personal income tax, now prohibited by Florida's constitution, with revenues tied to people investments by a "Human Investment Trust Fund." The fifth, presumably best, alternative combines the single business tax, the broadened sales and property taxes, and a personal income tax.

The 140+ page report gets to its conclusions laboriously and obscurely, presumably because the Florida Chamber wasn't comfortable with advocating them clearly. In simple terms, the report reflects some conclusions widely endorsed by tax experts and widely reflected in tax policies of other states including taxing personal income and avoiding massive erosion of the property tax base by homestead exemptions. Adopting these policies is clearly more of a challenge than Florida's governor wants to accept this legislative session.

Payroll Taxes In Nevada: There is a comparable issue in Nevada. The state's major teacher organization put a measure on the November ballot to adopt a corporate income tax. Many corporate and economic development leaders were opposed, along with the governor. But it wasn't clear that the measure would be defeated. The result was general agreement that the legislature would pass some sort of business tax in the 1991 session. The legislature is now considering alternatives comparable to those being discussed in New Hampshire. The base would be broad (e.g., total payroll) and the rate would be low (e.g., 1%).

Income Taxes In New Hampshire: New Hampshire officials have gotten into some exotic tax alternatives in an effort to raise money while relying heavily on a corporate income tax and avoiding a wage tax. The corporate profits tax inherently doesn't raise money from unprofitable corporations, a category including large corporations that

don't happen to make a profit in a particular year and smaller ones that don't make profits because they use up all potential profits as compensation for owners. The incentive to do this in the Granite State is very high as the profits are taxed but wages aren't. (Most states and the federal government set top bracket individual and corporate rates near the same percentage.) The latest New Hampshire proposal is a uniform business tax. The base would be: (1) profits, (2) wages and salaries, (3) depreciation, and (4) certain other items. It resembles a value added tax.

Common Problems Of The Three States: All these states have a comparable problem. Their tax policies inherently bear more heavily on business than the policies of other states. The lack of a personal income tax in all of them, a narrow sales tax base (and no tax in New Hampshire), and the narrow property tax base in Florida all lead to high reliance on business taxes. The net burden on particular businesses isn't necessarily greater in these three states than others because state and local spending is lower. But with the current configuration of their tax systems, these states find it hard to raise added money for education or budget balancing without further increasing business burdens or considering major new personal taxes - a personal income tax, a broadened base of the sales tax on consumer services, and higher property taxes on individuals. Avoiding these major taxes on households draws attention to ways to get more money from business. As a result, there is considerable interest in all three states in taxes closely resembling value added taxes, although state officials are avoiding the term "value added tax."

Another state that arguably has this problem is Texas. There the alternative to taxes affecting individuals -- broadening the base of the sales tax, a statewide property tax, or an income tax -- is expanding the base of the corporate franchise tax.

Taxing Value Added: On February 19, the U.S. Supreme Court decided a case (Trinova Corp. v. Michigan Department of Treasury) that some had expected might undermine Michigan's value added (single business) tax. Six justices sided with Michigan, two dissented, and recently appointed Justice Souter didn't take part in the case. The issue was how tax liability of multi-state corporations is divided among states. The court had long ago affirmed that the traditional three factor formula was fine for corporate income taxes. It attributes income in accordance with a state's share of a corporation's sales, property, and payroll. But the value added tax has a different base -- including interest, depreciation, and labor costs as well as income (profits). Trinova is an auto component supplier with only minor operations, but 26% of its sales, in Michigan. It claimed that the resulting substantial apportionment of tax liability to Michigan was unfair and violated the interstate commerce clause of the U.S. Constitution.

It is impossible to determine the extent to which constitutional concerns have been a barrier to value added taxes in states outside Michigan. However much it was such a barrier, that barrier has been eliminated. Value added taxes are probably also getting a boost from the poor performance of corporate profits, and thus corporate profits taxes, over the last several years. Interest has developed in value added, under other names, in Nevada and New Hampshire. This adds to past interest that has appeared in tax studies in states such as Texas and Louisiana. These factors suggest that value added taxes will be an increasingly serious state tax option.

A key factor in acceptance of the concept is likely to be the attitude of business itself. Some businesses, particularly manufacturing and utilities, could gain from a revenue-neutral shift to value added business taxes. To date, they have shown little interest in supporting such a shift. Many state officials would be reluctant to push a shift over united business opposition. Even in the midst of recession and fiscal problems, many state officials are reluctant to add taxes on business. Connecticut and Massachusetts provide examples among states that have traditionally had the most "liberal" policies, by just about any definition of liberal. As always, there are exceptions -- with the Pennsylvania governor's proposal to raise the profits tax (though to a level below where it once was) an example.

A standard business response is to consider that any move to value added taxes, federal or state, would be on top of, not in place of, burdens of existing taxes. Thus, Business Week (3/4) commented that the Supreme Court decision "has left corporate executives wondering whether revenue-hungry state governments will sock business with costly new taxes." The article quotes a staff member at the Council of State Chambers of Commerce suggesting there was "no question" that other states will be thinking of using the tax. The article concludes, "Corporations can only hope they do better in state legislatures than they did before the Supreme Court."

TAX POLICY ISSUES

Sales Tax Coverage: The report for the Florida Chamber seeks to compare the broadness of the base of the state's sales tax with that of other states. The measure is a crude one. Each state's sales tax collections are adjusted to reflect what would have been collected had the state taxed at 6% (Florida's rate). Local sales taxes are ignored. The resulting collections are compared to personal income. The results appear on Table 5.

The data mostly measure the broadness of the base of individual state sales taxes. However, they also reflect differences in spending patterns -- that is the proportion of personal income residents spending on taxed and untaxed services. Also, they reflect patterns of

tourism, with a New Yorker spending money in Hawaii appearing in the Hawaii tax numerator but the New York personal income denominator.

Table 5: Sales Tax Collection Potential At Uniform Rate
As Percent Of Personal Income, 1988

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	Hawaii	7.5%	18	Idaho	3.1%	32	West Virginia	2.4%
2	New Mexico	5.0	18	Iowa	3.1	35	Minnesota	2.3
3	Wyoming	4.6	18	Nevada	3.1	35	Ohio	2.3
4	South Dakota	4.3	21	Kansas	3.0	35	Rhode Island	2.3
4	Washington	4.3	21	Missouri	3.0	38	Illinois	2.2
6	Arkansas	4.0	23	Michigan	2.9	38	Vermont	2.2
7	Arizona	3.9	24	Nebraska	2.8	40	Connecticut	2.1
8	Georgia	3.8	24	Wisconsin	2.8	41	Massachusetts	2.0
9	Louisiana	3.6		United States	2.7	41	Pennsylvania	2.0
10	Mississippi	3.5	26	California	2.7	43	Maryland	1.9
10	North Carolina	3.5	26	Colorado	2.7	43	Virginia	1.9
12	Florida	3.4	28	Alabama	2.6	45	New Jersey	1.8
12	Indiana	3.4	28	North Dakota	2.6		Alaska	0
12	Tennessee	3.4	28	Oklahoma	2.6		Delaware	0
12	Utah	3.4	28	Texas	2.6		Montana	0
16	South Carolina	3.3	32	Kentucky	2.4		New Hampshire	0
17	Maine	3.2	32	New York	2.4		Oregon	0

Tax Burdens In Major Cities: The District of Columbia government has published its annual comparison of the tax burdens of the largest city in each state. The comparisons are made for families with incomes of \$25,000, \$50,000, \$75,000, and \$100,000, based on income, property, sales, and auto taxes. The top ten and bottom ten states in the comparison for income of \$50,000 are shown on Table 6.

Table 6: State And Local Tax As Percent Of Income, 1989
Largest City In Each State, Family With Income Of \$50,000

Rank	State	Percent	Rank	State	Percent
1	Wisconsin	14.8%	41	Arizona	6.9%
2	Oregon	14.6	42	Delaware	6.4
3	New York	12.3	43	Washington	6.3
4	Michigan	12.2	44	Tennessee	6.1
5	Pennsylvania	11.6	45	Alaska	5.2
6	Maryland	11.5	46	Nevada	5.0
7	Minnesota	11.1	47	New Hampshire	4.7
8	Iowa	10.7	48	Texas	4.6
9	Georgia	10.4	49	Florida	4.5
10	Ohio	10.1	50	Wyoming	3.6
	Weighted Average	8.5			

The tax burdens for different income levels can be compared to create a progressivity index for each city. The report does this, concluding that the most progressive overall tax structures are found in Louisiana, Minnesota, California, and Delaware. The least progressive systems are found in four states without personal income taxes -- Tennessee, Washington, South Dakota, and Texas.

Broadening The Income Tax Base: There are periodic proposals that state governments define their corporate and/or personal income tax base more broadly than the definitions used in the federal tax system. Broader definitions of taxable income have been reasonably common for corporations. Examples: "unitary" treatment of corporate income that encompasses some foreign income in the state tax base not included in the federal one and disallowance of accelerated depreciation in the early 1980s. There have also been examples in personal income taxes, such as refusing to allow exclusion of money contributed to IRA and Keogh accounts when they were first established. But taxpayer resistance and desires to reduce taxpayer compliance cost and ease state administrative costs and effort have tended to lead to conformity. So the state definition of income is usually no broader than the federal one. It is sometimes narrower as indicated by tax credits for corporations expanding employment and exclusion of Social Security payments from individual income.

Because states have been reluctant to tax income on a broader base than the federal government, there is a considerable state interest in future federal base broadening or narrowing. In this connection, Making America's Budget Policy: From The 1980s to the 1990s (M. E. Sharpe, 1990) is relevant background. Joseph Minarik (executive director, Joint Economic Committee) traces tax reform efforts in the Congress, emphasizing the tax reform legislation of 1986 which substantially broadened the income tax base. Although current Congressional interest in the subject isn't high, Minarik says, "The potential remains for significant broadening of the tax base." His candidates include tax-exempt industrial development bonds, employer payments for employee health and life insurance, upper income pension and salary reduction plans, and the exclusion of capital gains at death.

Property Tax Issues: In a year when most states are looking for additional revenue, property tax issues in general and property tax relief in particular wouldn't be expected to be major issues. But in some states they are. In Oregon, voters put the issue on the state agenda by requiring a phased reduction of local property tax for schools and mandating that the state replace the lost revenues. In Colorado, voters nearly approved a tax limit measure, drawing the attention of legislators to a similar measure to preempt another try for initiative approval in 1992. In Georgia, legislators put property taxes on the voters' agenda by a constitutional amendment calling for use-value rather than market value assessment. Voter approval gives the issue back to the legislature. A court decision in Utah requiring

equal treatment of state-assessed (e.g., railroad and utility) property and locally assessed (e.g., residential) property will require state implementing action. Both a court decision and constitutional amendment will lead the Nebraska legislature to consider property tax matters. Property tax relief has been a major issue for state leaders in Michigan and Wisconsin, but with no results so far. The issues will be revisited in those states, as well as in Kansas where it has ended some political careers and the governor wants to reduce property taxes by a third by broadening the base of the sales tax.

Sticking It To The Suburbs: The confluence of three "good government" concepts is producing a financial shock for residents and local elected officials in some major states. The state already affected most dramatically is New Jersey. Other states, particularly Connecticut and Pennsylvania, may soon follow. The three concepts are: (1) equalization in school finance, (2) state absorption of income-maintenance and other costs falling disproportionately on some areas, particularly central cities, and (3) increases in taxes while avoiding regressive impacts on the poor. New Jersey combined the three concepts: (1) distributing new school aid to favor poorer areas at the expense of rich suburbs, (2) raising money from an income tax increase on higher income persons, and (3) spending much of the new money on low income persons by (a) absorbing local costs disproportionately felt in low income communities and (b) targeting property tax relief to lower income residents. The result has been a tax revolt, which may cause the toning down, though not reversal, of these policy decisions.

Connecticut governor's proposals would have much the same impact. Affluent suburban households will have much more liability for a new 6% tax on income over \$25,000 and sales taxes on gasoline, newspapers, clothing, and other items than they will save by a reduction in the sales tax and dividends and interest tax rates. State aid for schools would rise 8% in Hartford, a distressed central city, but would drop over 32% in its affluent suburb West Hartford. Pennsylvania faces essentially the same issue, but proposals for handling it aren't yet clear.

These issues appear in other states, but not in quite the same combination. For example, Texas faces the consequences of changing its school aid formula. But it may opt to pay the costs by a mechanism like expanding the sales tax to services with less redistributive impact than an income tax, although the statewide property tax now being considered would have a massive impact on suburban communities.

The case that state budget cuts disproportionately affect the middle class is made by a recent (2/18) U.S. News & World Report article, "States Under Siege: Financially Pressed Governors Turn Their Guns On Middle Class Benefits." Evidence: (1) concentration of school aid cuts on more affluent districts in Virginia, (2) middle class services affected by cuts such as roads, schools, parks, and more, (3) soaring

tuition at higher education institutions, and (4) attempts, such as those in Massachusetts, to deny Medicaid benefits to the middle class.

Development Incentives: Efforts to lure a United Airlines maintenance facility are producing tax concession measures in several legislatures. Oklahoma enacted several bills. One permitted Oklahoma County voters to adopt a 1% sales tax to finance the facility, which they have now done. Another provides various forms of tax exemption (e.g., for purchases of computers, parts, and fuels), and extends an investment tax credit. Virginia's legislature has passed similar incentives, without the local option tax.

REGULATION OF FINANCIAL INSTITUTIONS

Troubled Banks: The problems of financial institutions in the Southwest are being overshadowed by problems in the Northeast, particularly New England. Financial troubles of New England banks and increased regulatory concern over risky loans have discouraged lending. The New England governors have expressed concern that tight money is exacerbating the region's recession. The New York Times (2/17) assessed the most recent financial reports of 12,926 banks to identify those with capital shortages (capital less than 3% of assets) or large portfolios of nonperforming loans (more than 8% of assets). Many of these are relatively small banks (assets under \$100 million). Reports took only the largest banks on the Times list to produce the summary shown on Table 7 (next page).

Clearly, the banking solvency problems are highly concentrated in the Northeast, including some small states with some large problems. Much more money is involved in Connecticut (population of 3.3 million) and New Hampshire (1.1 million) than in Texas (17 million) or California (29.8 million). The shift in the locus of troubled financial institutions is not without irony. The bailout of savings and loan institutions used a national fund to deal with problems concentrated in the Southwest and California. Some Northeastern elected officials objected to what they saw as a massive regional subsidy. If the list on Table 7 is indicative of where Federal Deposit Insurance Corporation money, plus any appropriated bailout money, will go, the regional subsidy argument now cuts quite differently.

Insurance Regulation Cooperation Failure? The Wall Street Journal (2/15) reported developments with junk-bond laden First Executive Corp. and its insurance subsidiaries. It said the situation, "appears to be a blow to state insurance regulators." According to the story, regulators of some other states were angry at New Jersey regulators' decision to demand a security deposit from the company -- presumably strengthening the security of policyholders of that state at the expense of policyholders in other states and frustrating the efforts of a multi-state working group of state regulators. The next step was a secret demand for a security deposit by Massachusetts

regulators which became public when the company withdrew from doing business in the Bay State.

Table 7: Larger Problem Banks, September 30, 1990

State	Assets Involved (mil.)	Number Of Banks With		
		Low Capital	Many Bad Loans	Both
Massachusetts	\$21,230	5	8	5
New Jersey	15,859	0	1	2
New York	13,038	1	6	2
Connecticut	12,360	1	9	5
Pennsylvania	5,638	1	0	0
New Hampshire	3,368	1	4	1
Arizona	2,893	0	2	0
Texas	2,816	9	1	0
Maine	1,450	0	1	0
California	1,307	2	3	0
Rhode Island	971	0	2	0
Virginia	889	0	2	0
Florida	791	2	1	0
Oklahoma	399	1	0	0
Louisiana	303	2	0	0
Kansas	232	1	0	0
Illinois	163	0	0	1
Mississippi	148	1	0	0

A more sanguine view of state insurance regulation is provided by NCSL staffer William Warren in State Legislatures (January). He notes "state regulators and insurance executives agree that state regulation must be improved to prevent insurance company insolvencies." He expects insurance company insolvencies to be an important issue for legislators in 1991 as they seek "assurance that guarantee funds will protect policyholders without draining the state treasury."

Rhode Island Credit Union Bail Out: The Rhode Island legislature has approved the creation of the Depositors Economic Protection Corporation (DEPCO). The plan is for the agency to borrow \$300 million in order to pay depositors of institutions that couldn't meet their obligations. Per capita, the deposits in failed institutions were about \$1,000 and the state's fund is \$300. Half the \$300 million would come from bank loans secured by assets of the failed institutions. The other half would come from dedication of half a cent of the existing state sales tax. The plan avoids any immediate apparent pain to Rhode Island taxpayers, but as banking specialist Bert Ely comments, "It doesn't make any difference which pocket you take the money out of -- the taxpayer is going to take the hit."

When all the loans, special funds, and repayments are washed out over time, the present value of the loss to Rhode Island taxpayers

would appear to be on the order of \$150-300 million, depending on the value the marketplace ultimately puts on the assets of the failed institutions. The earmarking of revenue for DEPCO aggravates the state's serious fiscal problem, estimated at a shortfall of \$200 million, equivalent to over \$3 billion in a state the size of Florida or Texas.

Bailout Avoided Elsewhere? Texas is taking a lesson from Rhode Island. By order of the state's credit union regulatory body, all state-chartered credit unions must apply for federal insurance by March 1 and obtain it by the end of the year. As they convert, credit unions will withdraw their shares in the \$35 million state guarantee fund. The head of the state regulatory agency commented, "No matter how strong your private insurer is, there is still a perception by the public that it needs to be insured by the federal government." Half of the affected 287 credit unions had already reached the same conclusion and had started application for federal coverage. Similar conversions are apparently taking place in Florida, Georgia, Massachusetts, and Missouri. In Missouri, the conversion would be required by legislation that has already passed the House. In Georgia, the action is a result of a decision by the Georgia Credit Union Deposit Insurance Corporation to disband.

Federal Bank Regulation Changes: The Bush Administration and others are making proposals for comprehensive reform of federal banking regulation. Most of the issues are clearly federal -- the size of deposits to be insured, the extent to which banks can engage in other businesses, capital requirements, holding companies, and the like. However, many proposals would further preempt state banking controls by prohibiting states from barring banks from operating unless chartered or approved by the states. Industrial corporations can operate freely in other states but banks, in deference to state laws to protect depositors, cannot.

In a meeting with New England governors, federal regulators, including the chairman of the Federal Deposit Insurance Corporation, indicated that regulatory changes were in the works to improve the capacity of the troubled New England banks (see Table 7) to operate.

SPENDING "OFF BUDGET"

Budgeting is essential to the effective operation of modern government. ... It is not exaggeration to state that the capacity to govern depends on the capacity to budget.

Allen Schick, The Capacity To Budget

We rarely fix the roof when the sun shines.

Governor Mabus, State-Of-The-State, 1991,
discussing Mississippi budget reform

Introduction: One key tenet of state and national finance laws is that administrators cannot spend public money except pursuant to law. Adherence to this concept would drive spending decisions into the legislatures, usually through the budget process. In practice, considerable spending occurs under state auspices that never enters state budgets. Examples are: (1) spending by independent authorities in such fields as housing, toll highways, pollution control, hospital facilities, transit, sewage treatment, and waste recovery, and (2) spending of funds controlled by agencies such as attorneys general in legal settlements, public utility commissions in rate cases, and state university foundations.

Spending Outside The Budget: Considerable national attention has recently fallen on federal practices that take certain spending items outside of the regular budget. The current items of interest are costs of the Gulf War in general and those to be paid by other nations in particular, the costs of the savings and loan bailout, and the costs of a possible bailout of the federal deposit insurance system for banks. But, in general, the federal budget is much more inclusive than state budgets. Both federal and state budgets have a concept of a "general fund" that excludes such special funds as those for highways. Both the federal government and states have a concept of an "all funds" budget, but states have many spending items that are excluded from what is defined as "all." The exclusions have become issues in some states.

Major State Authorities: The largest off-budget spending by state governments is the spending of independent state authorities. Most of these acquire funds initially by issuing revenue bonds and then selling service to the public. The user charges pay operating and administrative costs and interest and principal on the debt. This is the concept of turnpike authorities, port authorities, authorities used by some states to provide utility services, transit authorities, and more. A variant is the financing authority which uses the state's authority to issue tax exempt bonds to finance industrial facilities, hospitals, housing, and pollution control facilities. Another variant uses the authority to finance government facilities -- local ones like schools and state ones like universities and prisons.

In some cases, the authorities have quasi-monopoly positions that allow them to generate revenues well in excess of their costs. This has been particularly true for the many turnpike authorities that have paid off their initial debt, authorities that own key bridges in cities like New York, and authorities with unique access to low cost supplies (e.g., hydropower in New York) or revenues (e.g., water and sewer charges in Massachusetts). These authorities become attractive for relieving fiscal problems by: (1) assuming responsibility for new functions, such as additional segments of roads or investing in economic development and/or (2) picking up additional costs, such as the presumed costs of overhead services by state fiscal agencies. In extreme cases, the state can sell an existing asset, like a road, to the

authority. Moves like these have characterized state fiscal plans in Massachusetts, New Jersey, New York, and other states.

Presumed "abuse" of the capacity of authorities to borrow has been an object of concern in New York. In his state-of-the-state address, the governor discussed an undisciplined borrowing process and specifically expressed concern over using the Urban Development Corporation to borrow for prison construction. The comptroller has proposed an amendment to the state constitution that would place a cap on debt outstanding, whether by authorities or direct state borrowing, unless voters approved a higher amount.

His amendment would also deal with the separate problem arising when authorities are unable to cover their obligations. This happened to New York in the early 1980s, with a decision made that general fund money would be used to pay bondholders in order to protect the state's credit. The comptroller's amendment would eliminate "moral obligation" financing.

Money Not Entering The State Treasury: State constitutions and laws requiring appropriations typically apply to funds held by the state treasurer or "state funds." Those seeking to avoid the appropriations process (and the controls over purchasing and public disclosure that go with it) need to find a way to collect and disburse money without falling within such definitions. Some categories:

- o Organizations which themselves are not government but which may receive and spend public funds much as a contractor or grantee would do. Examples are inaugural committees, endowments such as those for the arts or wildlife preservation, quasi-public corporations such as Minnesota's Business Partnership, and more.
- o Organizations that are clearly state government but which establish other entities that receive and disburse funds without ever considering them government receipts. The simplest example is the office coffee fund, but there are more important others such as university foundations and student activity funds.

Off-Budget Financing In Maryland: The issue led to the February resignation of the Secretary of Health and Mental Hygiene, the state's largest spending department. The problem was legislative reaction to the management of the Maryland State Games Foundation, Inc., theoretically no more a state agency than an office coffee fund. The Foundation was established as a private nonprofit entity to raise money for various sports competitions. But its executive director was the state employee who headed the health department's state games project and office space was provided by the state. The Foundation's income came primarily from state grants. It allegedly misspent money

by renting a beach condominium, paying an employee while in jail, and in other ways.

Off-Budget Financing In South Carolina: Alleged abuses, such as renting \$800-a-night hotel rooms, by the Carolina Research and Development Foundation led to the resignation of the University of South Carolina president last year. This year a new problem has caused the governor to ask the state police to investigate. After some local news organizations won their suit to get access to the Foundation's records, they found many of the records had been destroyed.

Off-Budget Financing In Virginia: Governor Wilder's inauguration was an immense financial success, reportedly leaving about \$1 million which the governor plans to use as personally controlled funds for such purposes as assisting in election campaigns and, some say, running for President. He has refused to release information on who gave how much to the inaugural committee, reflecting the perspective that it was a purely private body. Taking the position that the inauguration is a state function, the legislature passed a bill requiring that future statewide elected officials disclose inaugural contributions and spend money only on inaugurations, but they would be permitted to keep any residual as campaign funds, not turn it over to the general fund as provided by an earlier version of the legislation.

The Politics Of Foundations: State officials have found handling the foundation issue to be tricky. On the one hand, the foundations often get money from state government. When they don't, they get money because of a relationship to something a state does support, such as a state university. This argues for auditing by the state, if not appropriations or purchasing and conflict of interest controls. On the other hand, most of the foundations do live out of donated money. The issues often pit heavy hitters in state politics as foundations are typically closely associated with state universities, economic development, public broadcasting, and governors' mansions.

Off-Budget Spending And Budget Reform: Allen Schick's, The Capacity To Budget (Urban Institute, 1990) is an assessment of federal, not state, budget processes. But it reflects criticisms of budget processes which many states share with the federal government. His summary comments reflect concerns of budget professionals with devices like off-budget handling of government spending.

When budget procedures are stable, one can be reasonably confident that the same rules for estimating the budget effects of legislative decisions will be continued from year to year. Stability in scorekeeping rules is valued because it facilitates inter-year comparisons and enables those making the decisions and those affected by the budget actions to have confidence in what they are doing. Because legislative scorekeeping rules are self-enforced,

they are sometimes manipulated for short-term advantage. The machinations undoubtedly escalate when fiscal stress intensifies.

The integrity of budget accounts is at great risk when the scorekeeping rules are made up each year... Without changing a single program or policy, deficits can be made to vanish or savings to materialize by changing the way transactions are accounted for in the budget. Placing items in or outside the budget, delaying or advancing payment dates, and manipulating the sale of assets are old tricks, but one has the impression that they have been used on a broader scale in the 1980s than previously.

LEGISLATIVE MANAGEMENT

Legislative Issues: Predictably, fiscal issues were named as the top priority in a new survey of legislative leaders. Education, particularly education finance, was ranked second. Third was the environment -- a complex of issues including solid waste, land use, and growth management.

Fourth, the leaders identified reapportionment and redistricting. Legislators handle their own redistricting in 39 states, with special boards or commission the pattern in the other eleven. Besides redistricting legislatures, the 44 states with more than one U. S. House member have to redraw Congressional districts. All but three of these states decide the issue in their legislatures.

NCSL President John Martin (ME) predicted "contentious 1991 legislative sessions." He also noted some of the legislative management issues not highlighted in the survey:

At the same time, legislatures face additional challenges as there are growing attempts to restrict the authority and options of legislatures through term limits and increased use of the initiative process. There also is a growing concern about campaign finance and ethics issues.

This article covers some of those topics including some aspects of legislative pay and its relation to tax treatment of expenses, legislative staff cutbacks, and various resources for dealing with legislatures.

Legislators' Taxes and Cost of Living Differences: A little known benefit of being a legislator is the special federal law dealing with legislator's expenses. Under the law applicable to everyone, legislators don't have to pay taxes on their ordinary and necessary expenses associated with doing their jobs. They don't pay these taxes because: (1) they account to the state on expense forms and are reimbursed only

for expenses they convince their employers to pay or (2) they don't file expense forms with their states, but do maintain expense records and deduct the expenses. The general rule for all taxpayers is that expense allowances paid without the submission of expense forms are treated as income, just like salary, though expense deductions can be taken against that income to the extent they exceed 2% of adjusted gross income. All taxpayers who spend considerable time at a job away from "home" and maintain any kind of residence at the job site (e.g., a permanent hotel room or shared apartment) run the risk of having IRS decide their tax home is where they work, so that no commuting expenses between "home" and the tax home (like a state capitol) are deductible.

Federal legislation permitting more favorable treatment for state legislators was enacted on a temporary basis in 1976, extended thereafter, and made permanent in 1981. Legislators who live more than 50 miles from the state capitol benefit from a special rule protecting them from having the state capitol declared as their tax home. Also, they can elect a special per diem rate. The rates are tied to federal employee per diems. Those currently in effect are shown on Table 8.

Table 8: Daily Per Diem Exclusions For State Legislators, 1991

Rank	State	Amount	Rank	State	Amount	Rank	State	Amount
1	Hawaii	\$126	18	Minnesota	\$82	35	Missouri	\$74
2	Massachusetts	121	19	North Carolina	82	36	Oklahoma	73
3	Alaska	117	20	Virginia	82	37	Florida	72
4	New Jersey	114	21	Wisconsin	82	38	Idaho	72
5	Georgia	108	22	Texas	81	39	Maine	71
6	Maryland	104	23	New Hampshire	78	40	Vermont	71
7	Rhode Island	100	24	Tennessee	78	41	Alabama	70
8	Colorado	99	25	Washington	78	42	Kentucky	70
9	New Mexico	99	26	Michigan	77	43	North Dakota	70
10	Connecticut	94	27	Iowa	76	44	Kansas	69
11	New York	89	28	Louisiana	76	45	Wyoming	69
12	California	88	29	Mississippi	76	46	Nebraska	67
13	Indiana	88	30	South Carolina	76	47	Montana	66
14	Pennsylvania	88	31	West Virginia	75	48	Nevada	66
15	Utah	86	32	Arkansas	74	49	Oregon	66
16	Ohio	85	33	Delaware	74	50	South Dakota	66
17	Arizona	83	34	Illinois	74			

Encouraging Longer Legislative Sessions: The federal law has a definition of the number of days the per diem may be claimed that creates strong incentives for "pro forma" or "skeleton" sessions and for committee meetings. Basically, a legislator may claim per diem when the legislature is in session, for short periods between session days, and for committee meeting days. The legislator does not need to travel to the state capitol to claim the per diem for a particular day.

The advantage of the arrangement can be substantial. Reports calculated the difference between normal tax treatment and the special rule for a hypothetical legislator and found a gain of \$5,000 to \$6,000. In Ohio, most Senators could deduct \$26,726 in 1990. The Senate had 121 session days arranged in such a way that they were deemed for tax purposes to be in session another 227 days, for total days of 348. The Boston Globe (2/3) checked the records of one prominent Massachusetts legislator and found that he claims state per diem for about 150 days a year, presumably the number of days he was on state business, but takes a federal tax deduction of about 360 days a year. In late January California's Board of Control approved increasing legislators' rate to match a recent change in the allowable federal maximum, permitting the maximum to rise to \$18,850 a year according to press reports.

Legislative Pay And Ethics: Texas legislators are under considerable pressure to adopt strict ethical standards, including prohibitions against taking things of value from lobbyists like vacation trips, entertainment, and meals. There has been press criticism of examples of these arrangements and others such as acceptance of retainers by lawyer-legislators. Texas has a larger-than-average problem in dealing with the many calls for stricter ethical standards. Many legislators feel that added job benefits are essential to recruit and retain legislators in general and part of their appropriate price of service in particular. In short, they feel underpaid. The result, according to the senator who is pushing one ethics bill: "You're not ever going to have a completely good ethics bill until you get salaries up."

Texas legislators are scheduled to be in session 140 days every other year. But they tend to meet in special sessions in the year no regular session is scheduled and to have issues with heavy time requirements as they have had the last several years with Workers Compensation reform and school finance equalization. By one compilation, the legislature has been meeting more often than the Congress. But legislative pay of \$7,200 a year was last changed in 1975. The last attempt to raise it -- which involves a constitutional amendment and thus a popular vote -- was in 1989, when voters rejected it by a 2-1 margin. As Texas legislators see it, they are serving the third largest state, but aren't getting compensated accordingly, as shown on Table 9 (next page).

Legislative Staff Layoffs: California's Proposition 130, the initiative approved by voters in November, required a reduction of nearly 40% in the legislature's operating budget (\$190 million) as well as limiting legislative terms. The announced staff reductions in the Senate are 200 of 1,000 employees and in the House 440 of 1,500 staffers.

Table 9: Legislator Compensation In The Ten Largest States, 1991

<u>State</u>	<u>Annual Pay</u>	<u>Per Diem</u>	<u>Other</u>
New York	\$57,500	\$75	
Pennsylvania	47,000	88	Plus \$10,000/yr. exp.
Michigan	45,450	0	Plus \$8,500/yr. exp.
California	40,816	88	
Ohio	38,482	0	
Illinois	35,661	74	
New Jersey	35,000	0	
Florida	21,684	50	
North Carolina	11,124	81	Plus \$465/mo. exp.
Texas	7,200	30	Out-of-session exp. allowance = \$85

Legislative staff who left voluntarily by January 31 got substantial benefits. First, they got four months severance pay with an extra month if they had more than two years service. For those who took other state jobs without a break in service, this produced some press criticism, but legislative leaders argued there was no basis for making severance pay less restrictive for those taking California jobs than those taking private sector jobs.

The legislature is challenging the initiative in court. The California supreme court has shown some willingness to reject initiatives as (1) covering more than one subject or (2) using the initiative process to make fundamental changes in the constitutional framework. This suggests the lawsuit has some prospect for success despite reluctance of the court to reject an initiative approved by voters.

Ethical Standards: The most recent Gallup Poll on ethical standards didn't rate state officials last, but didn't rate them highly either. Respondents were given a list of occupations and asked, "How would you rate the honesty and ethical standards of people in these different fields -- very high, high, average, low, or very low?" The percentage rating each group very high or high is shown on Table 10.

Table 10: Percentage Rating Honesty And Ethics High Or Very High

<u>Occupation</u>	<u>Percent</u>	<u>Occupation</u>	<u>Percent</u>	<u>Occupation</u>	<u>Percent</u>
Clergy	55%	Bankers	32%	Building Contractors	20%
Medical Doctors	52	Journalists	30	Congressmen	20
College Teachers	51	Business Executives	25	State Officeholders	17
Engineers	50	Senators	24	Labor Leaders	15
Policemen	49	Lawyers	22	Stockbrokers	14
Funeral Directors	35	Local Officeholders	21	Car Salesmen	6

State Government Relations: Leveraging State Government Relations is a 214-page compilation of materials developed by the Public Affairs Council (1019 19th St., N.W., Washington, DC 20036). Its concern is how corporate and trade association executives deal with "the newly powerful decision-makers in our state capitols who have assumed many of the political and governmental prerogatives once jealously husbanded by legislators in Washington and by federal regulatory agencies." Most of the essays deal with the profession of state government relations for the corporation -- how to do it, how to get cooperation within companies, how to monitor legislation, how to measure the results, and more.

The interest in state government relations has increased apace with the increasing number of decisions being made in state capitols. This is hard to quantify, although the Wall Street Journal used comparisons of the number of registered lobbyists in an article last year (5/30). For example the number of lobbyists registered in Iowa doubled between 1984 and 1988 while the number in Washington and Wyoming grew by a third.

The Government Research Service (701 Jackson, P.O. Box 2041, Topeka, KN 66601) has issued the sixth edition of its State Legislative Sourcebook. It is summarized in one of the essays in Leveraging by Margaret Rita (Tobacco Institute):

If you are responsible for monitoring and tracking legislation, you should have it. It contains all the basic information you need on a state's legislative organization, length of sessions, where and how to get bill copies, and so forth. It also contains the telephone numbers of the state capitols, bill status and reporting services and local contacts for information which official state offices do not readily provide.

The firm also publishes a bibliography of state "blue books" and similar publications that list state officials, facts about a state, telephone numbers, statistics, and other information which varies from state to state. For those wanting even more detail on sources of information about legislatures, it publishes a newsletter, Legislative Information Alert.

Tracking And Predicting Legislation: NCSL has released Enactments 90 -- no analysis, little description, but citations of laws passed by state legislatures last year. The document is impossible to use without supplemental sources because it gives only the subject matter of action (e.g., "Arts In Education, Funding") not the action (e.g., increased, decreased). State Issues 1991, also from NCSL, reflects 1,400 survey responses from legislators and legislative staff. The result is a compilation of elaborate statistical matrices of states and issues, highlighted by short summaries prepared by the NCSL staff. The problem with a survey of so many people on so many issues is that the results can tell readers less than they knew already. For example, the survey

results indicate, "arts agency funding will claim the attention of lawmakers in 38 states in 1991." The actual number is likely to be 50, as arts budgets will be voted upon or previously enacted budgets or earmarking will be at risk from budget cuts in every state. The missing 12 responses may suggest more about the survey than about arts funding issues. But by ignoring much of the 114 pages, readers can concentrate on what remains -- about a 25 page booklet by the NCSL staff summarizing this year's issues, a useful summary for many readers just to get a feel for the overall legislative agenda.

MISCELLANY

California Water Rationing: "I will not hesitate to assume emergency powers if such powers become necessary to protect Californians from the worst effects of the drought," said Governor Wilson in a mid-February press conference. The actions being considered, such as controlling water use from privately owned water sources, are a reminder of the inherent police power of state governments. For the moment, the governor is seeking to establish a \$100 million drought fund, encouraging communities to cut their water use, and establishing a voluntary "water bank" to transfer from those who may be willing to sell (e.g., rice farmers) to those who want to buy (e.g., municipal water suppliers short of water because their supplies from federal and state reservoir and aqueduct projects are being cut). The drought, besides being a problem in its own right, is likely to add to the state's fiscal problems by increasing spending and cutting into revenues from water-related activities like farming.

Disappearing Budget Cuts: As in 1982-83, many of the announced budget cuts aren't being fully implemented. Obstacles include: (1) reconsideration by governors in light of objections, (2) granting of large numbers of exceptions, (3) conflicts with collective bargaining agreements, (4) litigation, particularly in social service programs, and (5) lack of legislative approval in circumstances where it is required.

The record for reconsideration by governors is probably being set by Governor Schaefer of Maryland. He has announced and reconsidered: (1) cutting back general assistance (state-funded welfare), (2) reducing kidney dialysis services, (3) eliminating youth camps, (4) forcing state workers to put in a 40-hour week, and (5) laying off over 1,000 workers. Critics suggest he is trying to build pressures for a tax increase. The record for having FY 1991 cutbacks tied up in the legislature is being set in Maine where the legislative leaders (D) and governor (R) have sharply-differing ideas about appropriate ways to close a massive deficit.

Divestiture: California's health director has asked the trustees of state universities and state retirement systems to divest their portfolios of stocks of tobacco companies. Such action has been taken by a few universities (e.g., City University of New York), but Reports is unaware of any pension plans that have made the move. Divestiture of stocks of companies operating in South Africa remains an issue in some states (primarily state universities) and a policy in others. There are a variety of other issues where divestiture is suggested (e.g., munitions manufacturers, companies operating in Northern Ireland). The impact of such moves on the policies involved (e.g., apartheid, tobacco production) isn't easily measured.

The economic returns are in from nearly a decade of divestiture of securities related to South Africa by some states and experience of mutual funds which avoid or select securities for social policy reasons. Those results confirm what economic theory would suggest. So long as those selling (or buying) securities for any non-economic reason is small relative to total buyers and sellers, the actions of the other market forces will offset the actions of the few. As a result, proponents and opponents of divestiture in any particular state claim too much. There isn't a noticeable impact on companies' ability to raise equity capital and thus no economic pressure, though there may be psychological pressure. Also there isn't a loss in the rate of return realized on pension plan or university endowment portfolios, though there are one-time transaction costs if securities are sold as distinct from new purchases being avoided.

Federal Impacts On State Finances: A suit recently filed by Kansas against the U.S. Department of Agriculture is a reminder of concerns of state officials that the federal government uses its power to reduce the price of its operations by exemptions from state and local taxes. To the extent this happens, it requires higher taxes on everyone else. Examples are the mandate that states not apply their sales taxes to purchases made with Food Stamps, mandated exemption from sales taxes of sales to the federal government, and protection against property taxes accorded certain government contractors. The Kansas concern is over the private insurance companies that write about 85% of the crop insurance policies. In June, the Federal Crop Insurance Corporation issued a regulation that the private crop insurers would henceforth be exempt from state regulatory requirements and premium taxes. The decision will cost Kansas about \$500,000 a year.

Income Taxes: The governor of Tennessee recently joined the governor of Connecticut in proposing a personal income tax in a state that has been avoiding one. Both proposals would lower sales taxes on which the two states have been relying heavily.

Items: Louisiana's tax-free shopping program is now more than a year old. The concept is to rebate the substantial state and local sales taxes to foreign visitors who buy in Louisiana. The program gets a favorable review from the New Orleans Times-Picayune (1/27), which

concludes it has drawn considerable extra business. North Dakota has a similar plan for visiting Canadians. Maryland's Governor Schaefer turned what might have been an isolated decision into a lame-duck governor into what might become a trend when he followed Ohio former Governor Celeste's lead in pardoning a group of women convicted for killing or assaulting men who had battered them. For details and speculation on action by other states, see the New York Times (2/21).

TECHNICAL NOTES

Higher Education: The data on appropriations per student and percentage of operating costs paid by tuition are from Research Associates of Washington (2605 Kingle Rd., N.W., Washington, DC 20008), State Profiles: Financing Public Higher Education 1978 to 1990. This 217-page volume is an outstanding reference for state-by-state data on all aspects of higher education finance.

Tax Recommendations For Florida: The Florida study was commissioned by the Chamber of Commerce Foundation (136 S. Bronough St., P.O. Box 11309, Tallahassee, FL 32302) and performed by SRI International. The study of Florida's economic development potential and tax structure was published as a 143-page report, Crossroads: Designing Florida's Tax Structure.

Large City Tax Burdens: Tax Rates And Tax Burdens In The District Of Columbia: A Nationwide Comparison is produced by the Office of Economic and Tax Policy, Department of Finance and Revenue, Government of the District of Columbia, 300 Indiana Ave., N.W., Washington, DC 20001. The new data closely resemble the previous year (States In Profile, Table D-25 and, for the progressivity index, Table D-26). Particularly for the lower income household comparison, the data are extremely sensitive to assumed housing values. Families with income of \$50,000 are assumed to live in a house worth \$125,597 in the median state. The assumed value was only \$61,000 in Detroit and \$72,000 in Philadelphia but \$247,000 in Los Angeles and \$275,000 in Honolulu.

Legislative Management: The views of legislative leaders appear in Leaders' Outlook 1991, the result of an NCSL survey of state legislative leaders. The per diem tables are from the NCSL publication Issues In State Legislators' Income Tax. NCSL maintains a constantly updated table of legislative pay and per diem for the 50 states. The ten state version used in Texas and appearing in this issue is from the Austin American-Statesman (2/4). The ethical ratings are from a Gallup Poll in early 1990. It was reported in The American Enterprise (January/February 1991).

SPR

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Many of the state fiscal problems are being shifted to local governments, sometimes with relief from mandates or new local option taxing authority.

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Federal aid has become a less important factor in state budgets, but still redistributes purchasing power among states. Federal mandates remain a factor contributing to state budget problems.

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FISCAL DEVELOPMENTS

Introduction: Fiscal problems are proving more intractable than many state officials asserted in their campaigns and reaffirmed in their post-election comments. With no economic improvement and frustration of attempts to balance current year budgets, some FY 1991 deficits will carry over into FY 1992. In FY 1992, "structural deficits" and left-over FY 1991 problems combine to make sharp cuts necessary if tax increases are to be avoided.

Balancing FY 1991 Budgets: In December and January, governors in over half the states announced austerity measures to bring their current year budgets into balance. Some parts of these plans aren't producing the savings promised when they were announced.

Plans that have the effect of cutting employee wages have run into problems nearly everywhere. The New York plan for furloughs evolved into a plan for wage deferral. In Rhode Island, where about 85% of workers are unionized, the governor's plan for pay deferrals is opposed by the labor organizations which are seeking to block it in court. The governor is threatening to increase the number of layoffs, as well as shutting down government 36 days in the next 16 months if the plan is blocked. The first one-day partial shutdown of state activities occurred in March. In Massachusetts, Maine, and several other Northeastern states, the overall picture is comparable, but the details are different. The key difference between the furlough plans and partial shutdowns of state activities is that large numbers of workers, like corrections officers, would typically be exempt from the shutdowns.

Other budget cutting measures are experiencing problems as well, with litigation often delaying if not preventing reductions in welfare, Medicaid, and social services. In some states, like California and Maine, legislators have been reluctant to accept cuts recommended by governors.

In many states, the revenue news hasn't been good either. There are major downward revisions in California and the Northeast, while examples of unexpected revenues in other states are rare.

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Balancing FY 1992 Budgets: In the larger states, not many final new (FY 1992) budget decisions are being made this spring -- the seasonal hiatus between governors' presentations of budgets and final legislative decisions on spending on taxes. But news is trickling in that will affect the outcome. Most of it is bad. All of the bad news affecting FY 1991 carries into FY 1992. Any FY 1991 shortfall enters FY 1992 automatically as a lower balance (or larger deficit). The problems affecting FY 1991 -- litigation, factors causing lower-than-expected revenue, growing caseloads, etc. -- usually will affect the FY 1992 projections as well.

A complicating factor is the environment in which the FY 1992 cuts are being considered. Policies, such as across-the-board cuts, may seem acceptable when implemented for several months as temporary measures to restore budget balance. But they may be less acceptable to constituents, legislators, interest groups, and agency heads when considered on a full year basis. There are wide gaps between governors' FY 1992 spending reduction plans and what may prove acceptable to legislators in California, Maine, Massachusetts, and Michigan -- as well as other states.

Structural Deficits: Current state fiscal problems aren't temporary recession-related ones according to new looks at the future in several states. These states are instead facing "structural deficits," persistent tendencies for spending for existing activities to outrun revenues from current taxes. In New York, the budget office's five year review shows particularly rapid growth in foster care, education of handicapped children, and Medicaid. In Massachusetts, the governor has been discussing a structural deficit, reflected in the fact that the state has been running unbalanced by \$500 million to \$1 billion for each of the last three years, despite tax increases.

The argument that a "structural deficit" exists is stronger in California than many other states. The underlying workload driving education costs, the number of students, is stable or dropping in many states. In California, it is rising rapidly, with a K-12 increase of 4.3% factored into the new budget. The sharp enrollment gain also appears in higher education with average annual increases over the past six years of just over 2%. On top of these problems driving spending, California's revenue growth is slowed by indexing of the personal income tax. Indexing is designed to prevent inflation from automatically increasing the percentage of income taken by graduated income taxes. It provides automatic increases in exemption and/or bracket amounts to reflect price level changes. The federal government and a handful of states use it.

In its assessment of the FY 1992 budget, the California legislative fiscal office looked ahead to FY 1993 and FY 1994, concluding that current service spending would grow 10% in each year. Current service revenue growth will be substantially less -- with how much less depending on economic assumptions. As a result, the

Legislative Analyst foresees a structural deficit of about \$5 billion in FY 1993 and over \$6 billion in FY 1994.

Legislative-Executive Roles: The need for cutbacks in approved FY 1991 budgets and for cost-cutting in FY 1992 is revealing long-standing disagreements about executive and legislative power.

One conflict is over the authority to set fees. Some states give the executive branch broad authority to set fees for such items as birth certificates, copies of tax returns, and applications for state permits. Others cover almost all fee decisions by legislation. Many states have inconsistent, but arguably appropriate patterns. They set economically important or politically sensitive fees, such as auto registration and hunting licenses, by statute but let the executive branch set other fees based on criteria like covering the cost of service. Some governors have been seeking more fee setting authority. The issue is a long-standing one in Massachusetts. Governor Dukakis (D) won broad fee-setting authority from the legislature (D-led) in 1988 as part of a temporary budget-cutting plan. Now Governor Weld (R) wants to repeat the process. The House Republican leader opposed the action in 1988 and announced he will oppose it again this year.

Legislative Sessions: Two states, Kentucky and Virginia, have concluded their legislative sessions for the year.

Kentucky had no regular session scheduled and, with a large tax increase last year, has no major fiscal problems. It has concluded a special session dealing with such subjects as Workers Compensation reform and tax breaks to promote economic development.

Virginia's major legislative sessions are in even-numbered years, with off-year sessions limited in length -- a limit the legislature this year voted to relax by seeking a constitutional amendment allowing recesses during the session. Governor Wilder and legislative leaders agreed to cut spending in the FY 1992 budget enacted last year rather than raise taxes. Much of the pain was taken out of the adjustments by measures that neither cut operating spending nor raised taxes: (1) increasing the assumed return on pension fund investments, (2) using lottery money to support the regular budget rather than special projects, (3) relying more on tuition and less on appropriations to support universities, and (4) selling the state's interest in a railroad.

Reorganization And Cost Saving: Reorganization is being pushed as a budget-balancing device by some governors and recommended in other states by special study commissions. Some of the common proposals are: (1) reorganizing Medicaid administration by putting it in a separate department or combining it with health functions while severing it from welfare functions, (2) reducing the number of agencies by eliminating some small independent boards and commissions and consolidating small professional licensing functions in an umbrella licensing/regulatory agency, and (3) replacing boards and commissions

with a single agency head. Other reorganizations -- such as those concerning elected v. appointed state superintendents of education -- are under consideration, but generally in the name of efficiency and education quality rather than cost saving.

Reorganizing Rhode Island: The Rhode Island Public Expenditure Council has an extensive list of recommendations. One is creating a chief state financial officer with control over budget, accounting, taxation, and auditing. Conversely, some New Jersey legislators are seeking to dismantle the office of treasurer, reasoning that the excessive power of the office which has many of these functions led to the unpopular tax increase and local aid changes made last year. Other RIPEC recommendations: (1) a management information systems czar, (2) a cabinet council on human services, (3) a biennial budget, (4) consideration of a department of public safety, and (5) improved personnel management with many suggestions for how to achieve it.

Reorganizing West Virginia: Some reorganizations reflect principles long in effect in other states without apparent problems. For example, this year the West Virginia legislature is processing legislation to merge the beer commission and the liquor commission. The governor has administratively already achieved one economy by appointing the same individual as the head of both agencies.

Reorganizing Mississippi: Mississippi's governor pushed reorganization in 1989, suggesting that over \$30 million could be saved. The legislature adopted part of his plan including creating a Department of Administration and Finance and a Department of Human Services, each consolidating a number of smaller agencies. While the governor points with pride to the actions taken and says they have held down cost, observations by legislators and the Performance Evaluation and Expenditure Review Committee suggest that cost changes associated with reorganization are inherently minor unless major changes in the number of personnel are involved, which they haven't been so far.

Reorganizing Maine: While Mississippi implements its Department of Human Services, Maine legislators are considering dismantling their Department of Human Services to create new agencies -- a Department of Families and a Department of Health and Rehabilitation. A Department of Families bill was passed last year but vetoed by the governor. Both the legislature and the governor have produced commissions examining what to do next. Maine legislators are also considering a proposal that would reunite the financial and administrative functions that were split in 1986. Along with practically all budget and finance issues, reorganization has become a partisan issue in Maine between the legislative majority (D) and the governor (R). The governor is currently pushing creation of a "Commission on Government Efficiency and Organization" that would consider reorganization issues and report next year.

Reorganizing New Jersey: Massive claims are being made for the benefits of the reorganization of New Jersey government recently proposed by the governor. The plan is supposed to result in elimination of 3,000 jobs, plus about 38 staff members and hundreds of volunteers that would be affected by eliminating about 50 boards and consolidating another 20. The major shifts: (1) combining environmental protection and energy, except public utility regulation, (2) merging personnel functions into the Treasury Department, which has budget as well as traditional treasury responsibilities, and (3) combining financial regulatory agencies with commerce department functions. Consolidating business regulatory activities in a commerce department is one of Governor Engler's proposals in Michigan.

College Closings: State budget stringency, higher tuition, and relative stability in enrollments at levels sometimes below expectations of campus planners have produced some interest in closing college campuses as an economy move. However, closings are rare. The local campus is a matter of civic pride and a symbol of economic development for the local community and its legislators. It impacts some students, however few, whose education plans would be dislocated by closing. An argument is often made that the savings from closings would be minimal, because roughly the same number of students would have to be taught somewhere else at state expense. In states with predominantly white and predominantly black institutions, there is often fierce opposition by the alumni, staff, and students of the predominantly black institutions to mergers. This opposition has prevented implementation of merger plans in Louisiana despite strong support from the governor.

There are a few states with active college closing issues. In West Virginia, the perpetual dispute over whether the state needs, or can afford, three medical schools is coming to a head in this year's budget process. In Massachusetts, the governor has established a commission to examine closings. A transition report to the governor suggested closing several community colleges and the Massachusetts Maritime Academy. In North Dakota, the state institutions are listed in the constitution. A state supreme court decision holds that any institution listed must be "adequately funded." This prevents consideration of changes in a state where there have been major population declines, so a proposal to take institutional names out of the constitution is again before the North Dakota legislature this year.

Health Care: Interest in "bootstrap financing" of Medicaid continues with the proposal of Florida's governor to raise the tax on hospital receipts from 1.5% to 3.5% with funds to be used for indigent care. There is local debate over whether the proposal can be considered a tax increase or not. The governor calls it a hospital assessment. Arkansas is in the process of enacting what amounts to a state tax on the state share of Medicaid reimbursements to hospitals, with proceeds to be plowed into matching more federal Medicaid money.

West Virginia's House passed by voice vote a bill dealing with a "Disproportionate Share Fund." Kentucky's governor recently signed a bill taxing health-care providers to provide the state with money to match federal Medicaid funds.

The types of health care proposals that have been considered by legislatures over the past several years are being reintroduced, though with much less chance of enactment in the current fiscal environment. One type, with broad labor support, emulates the Canadian system and requires substantial added funding to cover the uninsured, usually proposed to be financed with a payroll tax. An example is "Universal Health Insurance for Ohio," legislation sponsored by 29 Members of the Ohio House. Its sponsors claim that it would cost \$23.8 billion a year compared to current costs of \$27.5 billion, though consumers would presumably buy some discretionary health care services, like cosmetic surgery, over and above the plan. Every Ohio resident would be a plan member entitled to free services. While service would be free the plan wouldn't -- requiring a 9% payroll tax on employers, a 1.25% payroll tax on employees, a big hike in alcohol and tobacco taxes, and resources now flowing through Medicare and Medicaid.

Another type, usually backed by health care providers, makes little or no change in the health care system but puts more money into it. "Health Access Florida," from the Florida Medical Association, is an example. It calls for increased state spending for Medicaid and reduced state revenues as a result of new employer tax credits.

One of West Virginia's major issues this year illustrates the complexity of state involvement in hospital rates. The state is one of those that has retained state rate-making with legislation up for renewal this year. Mountain State Blue Cross is campaigning, including spending about \$1 million in advertising, against state rate-setting. The organization calls it price fixing. The hospitals, traditionally opposed to rate ceilings, have reversed their prior position to support continued state control. Their concern is that Mountain State would use its buying power to force concessions in hospital rates.

Tax Increases: This will be a big year for state tax increases according to a new assessment by State Budget & Tax News (3/11). The publication predicts that major state tax increases will affect 62% of the nation's population through actions by about half the states. It suggests there will be no dominant pattern in which taxes are chosen for increases -- with business taxes, personal income taxes, sales tax rates, and broadening of the sales tax base all playing a part. The predictions imply that there will ultimately be major increases in about eight states where the governor hasn't proposed increases.

Two legislatures have already increased taxes. Rhode Island increased the personal income tax (from 23% of federal liability to 27.5%), the corporate income tax (11% surtax on present state liability),

and the gas tax (26 cents, up five cents). The scheduled reduction in the sales tax was also eliminated. Arkansas raised the sales tax and motor fuel taxes.

Sales Tax On Services: The Massachusetts sales tax on professional services (e.g., attorneys and accountants) remains a subject of controversy. No other major state has such a tax, but proposals for similar measures have been offered elsewhere.

The tax was enacted over business opposition last year, as part of the unsuccessful efforts to balance the Bay State budget. In his campaign, Governor Weld (R) included a pledge to seek its repeal. He sought repeal before the tax was scheduled to become effective. Instead, the legislature deferred the effective date until March to consider it in the context of the governor's budget recommendations. The governor presented a budget which legislative leaders (D) saw as raising questions about whether some of the revenue raising devices and proposed cuts were appropriate. They sought legislation deferring the effective date until July, also to wait to get a feel for the state's overall fiscal position. The governor pressed for outright repeal and won.

The governor maintains that the state budget can be balanced without the service tax and without any replacement tax. Some legislators are concerned that the budget recommendations achieve balance by shifting costs to subsequent years by devices like lower pension contributions and what amounts to sale-leaseback of state assets. Local officials are concerned that the budget avoids state tax increases only by cuts in local aid that will force local tax increases. Those interested in state spending for education, social services, and other state functions argue that cuts are too deep. As a result, it is possible that Massachusetts will increase taxes -- the state is still on SB&TN's TaxWatch. But repeal of the tax on professional services is likely to focus attention on other forms of tax increases, such as the increase in the sales tax rate that has been proposed by some interest groups.

Tax Positions Of Organized Business: The willingness of some business organizations to support broad based taxes is underlined by a recent decision by the Illinois State Chamber of Commerce. Two years ago the Chamber fought the increase in the flat rate personal income tax from 2.5% to 3.0% and a proportional increase in the corporate tax. They passed, but controversy over whether the increase should be extended this year was a major factor in the 1990 gubernatorial campaign. Now the Chamber is backing extension. The Arkansas legislature appears likely to pass an increase from 6% to 6.5% in the top bracket corporate income tax rate that is endorsed by several business groups. Funds would be used for vocational education.

Income Taxes: The prospects for new state income taxes remain mixed. In Connecticut, a recent poll indicates 70% of the population

oppose the governor's proposal to begin taxing income. Governor Weicker is pleased with the reaction to his tax plan and budget cutting proposals:

Everybody is pissed off. Not one side or the other, but everybody. Now doesn't that tell you this plan is fair.

In Tennessee, the apparently well-orchestrated effort to provide a majority for an income tax seems to be on schedule. But the issue is quiet in other states for now. In New Hampshire, officials are looking for new ways to tax business. In Texas, the interest is in a regional property tax. For taxpayers and those interested in schools, plus a state supreme court seeking equity in school finance, the tax is the equivalent of a statewide property tax. Legislators hope legally it isn't, as such a tax would be unconstitutional in Texas. The lieutenant governor recently announced his support for a Texas income tax.

Twisting In The Wind: Many state officials think they are dealing with tough, indeed unprecedented, problems this year. But some problems look less onerous when compared to worse situations. In that spirit, the candidates for most difficult problems this year are: (1) New Jersey where elected officials have to explain how they have both a major unpopular tax increase and massive cutbacks in some state spending, (2) New York where extreme state and local tax burdens make another tax increase unthinkable, but past spending patterns made massive cutbacks unthinkable as well, (3) Massachusetts where the gulf between the governor and the legislative majority is massive, (4) California where the gulf isn't as large, but a solution requires a two-thirds vote, (5) Arizona where distrust of public officials is about as high as anywhere in the country, and (6) West Virginia where the economy simply won't support the level of public services of the past or of other states.

INDEX OF STATE ECONOMIC MOMENTUM

Introduction: The latest Index of State Economic Momentum (Table 1) confirms the relative deterioration of the New England states and the continuing strong performance of the West. The Index, prepared quarterly by Reports, reflects the economic conditions in each state relative to the U.S. average. It consists of the most recent annual rates of change in personal income, employment, and population of each state compared to the national average of those measures. A state with a growth rate 1% over the national average in each measure would appear in the Index as a +1.0. The national average is 0.0.

Table 1: Index Of State Economic Momentum, March 1991

Rank	State	Index	Rank	State	Index	Rank	State	Index
1	Nevada	5.78	18	Maryland	0.31	34	Connecticut	-0.80
2	South Carolina	3.83	19	Arkansas	0.27	35	Pennsylvania	-0.85
3	Utah	2.19	20	North Carolina	0.15	36	New York	-0.85
4	Washington	2.18	21	Ohio	0.14	37	Tennessee	-0.90
5	Arizona	1.82	22	Kentucky	0.09	38	Missouri	-0.92
6	Idaho	1.59	23	Georgia	0.04	39	Michigan	-1.00
7	Florida	1.46		United States	0.00	40	New Jersey	-1.13
8	Oregon	1.32	24	South Dakota	-0.01	41	Delaware	-1.14
9	Alaska	1.27	25	Kansas	-0.09	42	West Virginia	-1.14
10	Hawaii	1.14	26	Alabama	-0.29	43	Illinois	-1.15
11	California	1.13	27	New Mexico	-0.29	44	North Dakota	-1.32
12	Texas	0.77	28	Montana	-0.33	45	Wyoming	-1.38
13	Colorado	0.56	29	Iowa	-0.43	46	Rhode Island	-1.86
14	Minnesota	0.46	30	Indiana	-0.48	47	Maine	-2.12
15	Wisconsin	0.38	31	Oklahoma	-0.61	48	Massachusetts	-2.41
16	Nebraska	0.35	32	Mississippi	-0.76	49	Vermont	-2.48
17	Virginia	0.33	33	Louisiana	-0.76	50	New Hampshire	-2.77

Growth Patterns: Many economists believe that there is a tendency for a state's growth rate to move toward the national average over time. This argument is particularly valid at the high end. If a state continued to grow in population, employment and income long enough, it would become the nation and hence the national average. In this quarter, there is much wider divergence from the average than in the past. There are 23 states which deviate more than 1% from the national average, and 8 states which are more than 2% off. This is up from only 15 states last quarter, 6 of which were more than 2% off average.

Western states occupy the top 11 ranks with two exceptions. Florida continues to attract new residents which contributes to the state's ranking itself and stimulates personal income and employment. South Carolina's economy has benefited from the reconstruction efforts following Hurricane Hugo, so there has been strong growth in employment and personal income from hurricane-depressed levels, making its Index second only to Nevada's.

The bottom ranks are held by New England states, where unemployment has been rising and personal income lagging. Many other Northeastern states are in the bottom third in economic momentum which accounts for the poor performance of state revenues in the Northeast.

Employment Change: Nationally, employment in the past year grew by 0.5% about half as fast as typical annual population growth. Fourteen states experienced job losses, including some Southeastern states as well as Northeastern ones. The changes are shown on Table 2.

Table 2: Percentage Change In Employment, December 1989 And 1990

Rank	State	Change	Rank	State	Change	Rank	State	Change
1	Nevada	5.86%	18	Texas	1.70%	34	Mississippi	0.44%
2	Utah	4.74	19	Ohio	1.58	35	Missouri	0.22
3	Idaho	3.55	20	Montana	1.19	36	Pennsylvania	0.00
4	Washington	3.26	21	Louisiana	1.18	37	Georgia	-0.01
5	Arizona	2.81	22	Wisconsin	1.10	38	Delaware	-0.09
6	North Dakota	2.75	23	Alabama	1.07	39	Maryland	-0.11
7	Alaska	2.67	24	West Virginia	1.05	40	Tennessee	-0.34
8	South Dakota	2.67	25	Indiana	0.96	41	North Carolina	-0.37
9	Colorado	2.63	26	Iowa	0.93	42	Michigan	-0.90
10	Nebraska	2.58	27	Oklahoma	0.91	43	New Jersey	-1.08
11	Arkansas	2.52	28	California	0.90	44	Connecticut	-1.16
12	Oregon	2.43	29	Minnesota	0.90	45	New York	-1.51
13	South Carolina	2.35	30	Wyoming	0.88	46	Rhode Island	-2.59
14	Hawaii	2.32	31	New Mexico	0.72	47	New Hampshire	-3.14
15	Kansas	2.02	32	Illinois	0.57	48	Vermont	-3.60
16	Kentucky	1.90	33	Virginia	0.54	49	Massachusetts	-4.42
17	Florida	1.84		United States	0.53	50	Maine	-4.50

The big winners in employment were in the West. Fifteen states showed an increase in employment of more than 2% between December 1989 and December 1990, with Nevada continuing to report the largest gain (5.9%) and Utah the only other state with an increase in excess of 4%. Idaho, Washington, Arizona, and Colorado all showed employment gains of more than 2.6%.

Other Indicators: Reflecting the patterns shown in the Index, retail sales in the Northeast were down in November by 0.6% from a year earlier, while the U.S. average was up 3.9% and the West and Midwest were up 5.1% and 6.2% respectively. The Conference Board's Help Wanted Index indicates that the Pacific region is suffering an employment slowdown. According to a Conference Board economist "Declines in the Pacific region have increased to the point where they now match those in the hard pressed Northeast." Many economic indicators -- the unemployment rate, housing starts, and state revenues, for example -- show that the nation's slump has reached the California economy.

INDUSTRIAL DEVELOPMENT COMPETITION

Economic Development Scorecard: Site Selection (February) has just published its compilation of announcements of new industrial facilities and expansions in 1990. The information presents many different comparative measures (see Technical Notes). **Reports** likes new plant announcements as the single most useful indicator of how the states are doing in economic competition.

In terms of state shares of the total of 1,583 manufacturing facilities announced in 1990, Texas is the winner with 146 facilities. Runners-up are Florida (103) and North Carolina (102). But the position of these large states drops considerably when the new plants are related to population as is done in Table 3.

Table 3: New Manufacturing Plants Per Million Population, 1990

<u>Rank</u>	<u>State</u>	<u>Number</u>	<u>Rank</u>	<u>State</u>	<u>Number</u>	<u>Rank</u>	<u>State</u>	<u>Number</u>
1	Mississippi	35.2	18	Wisconsin	7.1	34	Minnesota	3.2
2	Kentucky	16.0	19	Oregon	7.0	35	Pennsylvania	2.7
3	North Carolina	15.3	20	Nebraska	6.9	36	Maryland	2.3
4	Alabama	15.0	21	Iowa	6.8	37	Wyoming	2.2
5	South Carolina	14.3	22	Ohio	6.8	38	Rhode Island	2.0
6	Oklahoma	14.2		United States	6.4	39	California	2.0
7	Georgia	13.7	23	New Hampshire	6.3	40	Colorado	1.8
8	Tennessee	13.3	24	Arizona	6.0	41	Alaska	1.8
9	Virginia	10.9	25	South Dakota	5.7	42	Hawaii	1.8
10	West Virginia	10.0	26	Illinois	5.7	43	Vermont	1.8
11	New Mexico	9.9	27	Louisiana	5.7	44	Maine	1.6
12	Missouri	9.3	28	Indiana	4.9	45	New Jersey	1.4
13	Arkansas	9.3	29	Utah	4.6	46	New York	1.2
14	Washington	9.0	30	Michigan	4.2	47	Massachusetts	1.2
15	Texas	8.6	31	Idaho	4.0	48	Connecticut	0.6
16	Florida	7.9	32	Montana	3.7	49	Delaware	0
17	Kansas	7.6	33	Nevada	3.3	50	North Dakota	0

The outcome shown by the table is striking. Southeastern states cop eight of the top ten positions with Oklahoma and West Virginia, which share some Southeastern characteristics, getting the remaining two positions. The Northeast and California occupy most of the bottom ranks.

Economic Development and Taxes: The rush to make tax concessions to lure economic development continues with the Kentucky governor's signature of a cap on jet fuel taxes to benefit Delta Airlines if it expands operations at the Cincinnati Airport, which is in Kentucky. State and local governments continue offering concessions to attract a United Airlines maintenance facility. A bill to exempt aircraft parts from the sales tax has passed the Colorado legislature.

The Colorado legislature is also moving a bill that would extend favorable tax treatment of coal mining. In the North Dakota legislature, several measures have passed the Senate to reduce the oil extraction (severance) tax. The House has passed legislation which would eliminate the tax for incremental increases in production, defined as all production through secondary and tertiary recovery methods such as injecting wells with water. Wyoming's legislature adopted a special 2% severance rate, one third the regular rate, for wildcat wells (ones in

new fields) by overriding a veto of the governor. Use of tertiary recovery would cut the severance tax from 3.75% to under 2% under a measure moving in the New Mexico House.

Oklahoma's legislature appears likely to pass legislation giving a sales tax exemption on construction materials to firms creating 100 or more jobs -- extending a concession previously granted for Kimberly-Clark to other firms.

South Dakota has acted to alter its taxes on banks with net income over \$500 million. The state doesn't have banks of that size in abundance, so the measure is understood to be designed solely as an incentive for Citicorp. The old law provides a tax of 6% of income. Under the new law, income under \$500 million is taxed at the old rate, but income above \$500 million is taxed at rates decreasing to 1% for income exceeding \$600 million.

Governor Weicker is selling his proposed new income tax as a good deal for business. "This is Christmas as far as the business community is concerned." He stresses the rollback of the corporate income tax and promised that when the deficit problem is solved he will seek to drop the rate further. He defends using a 6% flat rate rather than a graduated rate to tax personal income and reducing the tax on dividends and interest on the basis of keeping higher income persons, now "leaving in droves," in the state.

Industrial Development Exemptions And The Environment: Over thirty years ago, Mississippi began granting limited-term property tax exemptions for new manufacturing plants. The incentive was gradually copied throughout the nation. In the South, the exemptions, such as forgiveness of all property taxes on new facilities for ten years, are typically granted through state laws and state certifications. In the North, local governments generally have a greater role in the process. The exemptions make manufacturing operations cheaper but deprive local taxing jurisdictions of revenue. Because the exemptions, and their economic equivalents in other property tax concessions, are so widespread, there is no empirical way to show how important they may be in attracting development. {Comparing development in states with exemptions to development in states without is impossible if there aren't significant numbers of states without.} Those engaged in economic development believe that not having such exemptions would make their states non-competitive in drawing new investments.

The exemptions and their newer counterparts, like exemptions in enterprise zones, have their critics. There have been attempts to limit them in various ways: (1) requiring that new jobs be associated with the new investment, (2) limiting the exemption in amount and/or time for which it is available, and/or (3) limiting the taxes affected, such as providing the exemption for municipal and county taxes but not for school taxes. Louisiana is implementing a policy that seeks to tie the amount of the second five years of a ten-year exemption to avoiding

pollution, with higher polluting companies granted smaller exemptions. Some Louisiana business interests are critical of the change on the theory that it will retard economic development.

Financing Transportation: Many states are involved in the financing of freight railroads to deal with the threatened abandonment of branch lines. There are also some state subsidies of inter-city passenger rail. South Dakota, with its small population and large land area, has recently been subsidizing air passenger operations through the South Dakota Airline Authority. But, so far, use of routes to six cities (two others have been dropped) has been about a third of estimates. State officials are considering dropping the idea.

STATE AND LOCAL GOVERNMENTS

Dramatic Shift Underway: Although statistics aren't easily developed, a clear shift is occurring in the relationships among the federal government, the states, and general purpose local governments -- counties, townships, cities, towns, and boroughs. (As shorthand, this article refers to all these as "cities and counties.") The shift isn't affecting how states and the federal government relate to school districts and is uneven in its impact on special districts used for water supply, sewage, transit, and other functions. The emphasis is illustrated by Governor Cuomo's budget recommendations. They suggested cutting unrestricted aid in half while protecting school aid -- in relative terms -- with a 10% reduction.

The New York budget illustrates the tendency of budget recommendations in fiscally pressed states to single out local aid for cuts. In his budget message, Governor Cuomo dealt with a \$6 billion budget gap, with \$1.5 billion to be handled by tax and fee increases -- again deferring a scheduled personal income tax cut, university tuition and one time adjustments. This left a \$4.5 billion gap to be handled by spending cuts from current service levels. The proposed cuts are shown on Table 4.

While the allocation of New York cuts isn't strikingly dissimilar from the allocation of the base budget, Table 4 shows the large percentage of state budget cuts falling on local government. Identifiable regular local aid accounts for 43% of the cuts -- not including Medicaid which also goes to local government in New York and the portion of other programs benefiting local governments.

Table 4: Governor's Plan To Cut New York FY 1992 Spending (\$ mil.)

<u>CATEGORY/Activity</u>	<u>Amount</u>	<u>Percent</u>
State Operations	\$965	21.87
School Aid	891	20.2
Medicaid	875	19.8
Local Aid -- Unrestricted	468	10.6
Local Aid -- Restricted	530	12.0
Higher Education	128	2.9
Other Education (e.g., libraries, private colleges)	229	5.2
Social Services	175	4.0
Other	159	3.6
TOTAL	\$4,420	100.07

The essence of the shift is to leave cities and counties much more dependent on their own resources with less federal aid, less state aid in relation to total spending, and, in some but not all cases fewer mandates and more authority to raise money locally.

Measuring Local Aid: Total state aid to local government in FY 1989 was \$153 billion. This represents an increase of 8% over FY 1988, slightly above the 7.6% increase in state spending. State aid represents about 43% of all state spending, but the percentage varies substantially from state to state as shown on Table 5.

Table 5: State Aid As Percentage of State Spending, FY 1989

<u>Rank</u>	<u>State</u>	<u>Percent</u>	<u>Rank</u>	<u>State</u>	<u>Percent</u>	<u>Rank</u>	<u>State</u>	<u>Percent</u>
1	California	71.17	17	New Jersey	38.87	34	North Dakota	23.27
2	New York	59.4	18	Georgia	38.6	35	Maryland	27.8
3	North Carolina	54.3	19	Missouri	37.1	36	South Carolina	27.1
4	New Mexico	53.6	20	Pennsylvania	37.0	37	Iowa	26.4
5	Ohio	53.1	21	Wyoming	36.9	38	Connecticut	26.2
6	Arizona	52.5	22	West Virginia	36.8	39	Oklahoma	25.0
7	Indiana	50.1	23	Kansas	36.0	40	Alaska	24.4
8	Idaho	49.0	24	Washington	35.5	41	Massachusetts	23.9
9	Minnesota	47.1	25	Maine	35.4	42	Rhode Island	23.4
10	Florida	46.4	26	Tennessee	35.0	43	Oregon	22.1
11	Michigan	43.3	27	Colorado	32.8	44	Montana	21.1
12	Mississippi	43.1	28	Illinois	31.6	45	Delaware	19.8
13	Wisconsin	42.9	29	Kentucky	28.9	46	Nebraska	16.6
	United States	42.9	30	Vermont	28.7	47	New Hampshire	16.1
14	Alabama	42.6	31	Virginia	28.7	48	South Dakota	11.7
15	Utah	41.3	32	Arkansas	28.5	49	Hawaii	1.3
16	Texas	40.4	33	Louisiana	28.3		Nevada	n/a

The primary factor in determining the rankings on Table 5 is the division of functions between state and local governments. California and New York provide aid to counties for welfare -- aid that isn't provided in most other states because the state itself administers welfare. Conversely, Hawaii ranks last because it runs the schools. So it doesn't have a state school aid program.

Types Of Aid: While state aid of over \$600 per capita provides massive support for local governments on average, the support for cities and counties is much less significant. Table 6 breaks FY 1989 aid into its components.

Table 6: Composition Of State Aid To Local Government		
Type Of Aid	Amount (bil.)	Pct. Growth FY 1989
Restricted	\$136.7	8.2%
Education	\$97.6	8.4
Human Services	26.9	7.8
Transportation	6.0	8.5
Criminal Justice	1.8	19.9
Environment/Natural Resources	1.0	2.1
Community & Econ. Development	0.6	-17.3
Other Restricted	2.8	10.1
Unrestricted	16.6	6.3
Total	153.3	8.0

Some 64% of all state aid is earmarked for education. Another 18% is earmarked for human services, a mixed blessing for local government because local cost sharing of rising costs, such as New York's Medicaid program, is a price of the aid. Human service grants to local government is highly concentrated. Seventeen states don't provide such aid and 79% of all aid for the function is concentrated in California, New York, and Ohio. Adding all these, 82% of all state aid is of little value in financing core functions of cities and counties, that is, functions those jurisdictions perform in most states. Furthermore, the last column shows that the earmarked functional aid is growing faster than unearmarked aid.

Aid that isn't restricted by function consists primarily of large programs in a few states rather than widespread smaller programs in many states. For example, states distribute \$3,243 million as payments in lieu of taxes of which \$1,909 million is by California and \$665 million by Illinois.

Cutting Local Aid: In Massachusetts, a portion of the continuing state fiscal problems is being shifted to local government. The voters approved an initiative in November designed to ensure that the local

share of state revenues remains constant. But the legislature may override it to avoid a state tax increase. The governor's new budget calls for a cut of about \$270 million in local aid. The legislature is adopting measures that will make it easier for local governments to raise money including taxing auto sales and a liberalization of the limits of Proposition 2 1/2, the property tax limit. The governor has proposed eliminating mandates in fields ranging from special education to construction management.

To conserve cash, states have been routinely delaying payments to local governments in many instances. New Jersey did this in FY 1989. Legislation is being considered to delay again in FY 1990. The state collects business personal property taxes for local governments. The legislation would let the state hold the money, \$40 million, by shifting payment to local government from this spring to July.

The Impact On Local Governments: The National League of Cities recently released a consultant's economic report for its board which commented:

Changes in the intergovernmental system are increasing the fiscal squeeze on cities and towns throughout the United States. Federal cutbacks, current budget shortfalls in many states, and escalating mandated costs are increasing the fiscal burdens of cities and towns, even as many attempt to cope with the costs of economic and demographic change.

Facing such problems, cities and counties are looking for money and for relief from state and federal mandates increasing local costs. Their money interests include state and federal aid, metropolitan area financing, and increases in local option taxing authority by state legislation.

Meanwhile state and city-county problems are playing out in some major situations, including county finance in California (see below), financing Philadelphia, and financing New York City. New York City's fiscal situation would be serious even if the state maintained aid at current service levels. But the governor's budget cuts aid by \$400 million (according to the governor) or \$600 million (according to the mayor) -- or roughly \$60-90 per city resident. {It is generally agreed that the budget is tougher on other communities than New York with, for example, 20% cuts for school aid on Long Island and 2% in New York.} State officials are reluctant to do much more for the city which has recently granted 5% pay increases while the state is providing employees 0%.

Realignments Of State And Local Functions: Most of the activity in state-local fiscal relations this year consists of state-initiated reductions in traditional patterns of local aid. The trend toward state takeover of certain local functions -- general assistance, other

welfare and social services, and courts -- has been a victim of fiscal problems. Exceptions arise primarily in the context of increasing revenues. New Jersey's action last year involved takeovers of court and welfare costs, one of the aspects of the plan that made it particularly beneficial to low-income urban communities like Camden and Newark. In California, the governor's budget proposes shifting nearly \$1 billion in state costs for community mental health and public health to the counties. The offsetting revenue would come from altering the base of the motor vehicle tax (2% of market value) and from increasing alcoholic beverage taxes and giving the bulk of the new money to counties. As with federal proposals for "sorting out" federal and state functions, the proposal raises concerns about whether the new revenues will flow to particular counties in proportion to the increased spending responsibility and whether, as the Legislative Analyst suggests, the growth in spending is likely to be faster than the growth in revenues.

Limited Good News For Local Government: Not all the news from state capitols is bad news for local government finances. The proposals for broadening the base of state sales taxes, such as those in California, typically broaden the base of local option sales taxes automatically, and thus increase local tax revenues without local legislative action. Second, in limited instances, cuts in state programs cut local costs as well, with the Medicaid proposals in New York (e.g., some copayment by patients) the most prominent example. Third, officials of some states, such as Massachusetts and New York, are working to find ways to reduce state-mandated costs for cities and counties. In the name of education restructuring, officials of many states are trying to do the same thing for school districts.

Providing local governments with more revenue options is also popular. In Massachusetts, the door is being opened to property tax increases without some of the difficulties previously imposed by Proposition 2 1/2. In California, the governor has proposed a new half-cent county sales tax for law enforcement and moving from two-thirds to majority approval for school and jail bonds.

TRAVEL AND TOURISM

William Pound, the National Conference of State Legislatures executive director, says "an aggressive and creative approach to travel and tourism can pay big dividends to the states." To tap this potential, NCSL has just published Travel and Tourism: A Legislator's Guide. The 116-page volume asserts that travelers' spending accounts for 6.7% of gross national product, is the source of nearly six million jobs, and makes travel and tourism the third largest retail industry, outranked only by food stores and auto dealers.

States have quite different success in attracting the high-spending international tourist. Table 7, derived from a table in the NCSL study, relates the number of foreign tourists to state populations.

Rank	State	Number	Rank	State	Number	Rank	State	Number
1	Hawaii	223.0	17	New Hampshire	6.6	34	Michigan	2.9
2	Nevada	83.5	18	Connecticut	6.5	35	Idaho	2.9
3	Wyoming	31.4	19	New Jersey	6.5	36	South Carolina	2.8
4	Florida	25.9	20	Delaware	6.0	37	North Carolina	2.8
5	Arizona	23.7	21	Alaska	6.0	38	Ohio	2.6
6	New York	21.5	22	New Mexico	5.8	39	Wisconsin	2.5
7	Utah	18.6	23	Maine	5.7	40	Iowa	2.4
8	California	15.4	24	Georgia	4.5	41	Indiana	2.2
9	Massachusetts	13.6	25	Pennsylvania	4.2	42	Alabama	2.2
10	Colorado	10.4	26	Oregon	4.1	43	Kentucky	1.9
11	Louisiana	10.3	27	Texas	4.0	44	Nebraska	1.8
	United States	10.0	28	Tennessee	4.0	45	Kansas	1.7
12	Rhode Island	9.1	29	Minnesota	3.8	46	Oklahoma	1.6
13	Washington	8.1	30	Virginia	3.8	47	Arkansas	1.3
14	Illinois	7.8	31	Maryland	3.8	48	Mississippi	1.0
15	Vermont	6.9	32	Missouri	3.4		North Dakota	*
16	South Dakota	6.8	33	Montana	3.4		West Virginia	*

* Not Enough To Make The Count Reliable

The table suggests that the economic benefits of international tourism are highly concentrated in a few states. These are Hawaii, a popular beach destination for Japanese as well as Americans, gambling in Nevada, New York City, and some of the major national parks and theme park locations. Most states are well below the national average. Mexican and Canadian tourists (not shown in the table) concentrate their trips in neighboring states like Texas, Maine, and Michigan.

The report provides examples of state targeting of overseas tourists, such as marketing to British and German tourists by South Carolina. A few states have substantial budgets to promote foreign tourism, particularly Florida, Hawaii, and Illinois. Each spent over a million dollars for this purpose in FY 1989. This doesn't include the many state outlays for highways, historical sites, and state parks. Most state outlays for travel promotion are oriented to domestic tourism or, as with brochures, have no particular geographic orientation. Travel office budgets for the 50 states were \$341 million in FY 1990. The biggest spender is Hawaii (\$22.5 million) followed by larger states like New York, Illinois, Texas, and Pennsylvania. California is an exception. The largest state in population had the

20th largest travel budget. Travel budgets per capita are shown on Table 8.

Table 8: Travel Office Budgets Per Capita, FY 1990

<u>Rank</u>	<u>State</u>	<u>Amount</u>	<u>Rank</u>	<u>State</u>	<u>Amount</u>	<u>Rank</u>	<u>State</u>	<u>Amount</u>
1	Alaska	\$20.62	18	Illinois	\$1.92	34	New York	\$1.22
2	Hawaii	20.20	19	New Hampshire	1.90	35	Louisiana	1.22
3	Wyoming	8.57	20	Minnesota	1.84	36	Missouri	1.18
4	Montana	5.65	21	New Mexico	1.79	37	Massachusetts	1.16
5	South Dakota	4.57	22	Wisconsin	1.73	38	Texas	1.11
6	Nevada	4.24	23	Maine	1.69	39	Oregon	1.07
7	Vermont	3.55	24	Virginia	1.66	40	New Jersey	1.03
8	Arkansas	3.26	25	Iowa	1.60	41	North Carolina	0.96
9	Rhode Island	2.80	26	Arizona	1.51	42	Nebraska	0.94
10	South Carolina	2.47	27	Michigan	1.51	43	Mississippi	0.88
11	North Dakota	2.42	28	West Virginia	1.50	44	Kansas	0.86
12	Colorado	2.37	29	Maryland	1.38	45	Florida	0.73
13	Idaho	2.29		United States	1.37	46	Connecticut	0.60
14	Tennessee	2.17	30	Kentucky	1.37	47	Washington	0.55
15	Utah	2.14	31	Pennsylvania	1.33	48	Indiana	0.54
16	Delaware	2.10	32	Georgia	1.27	49	Ohio	0.49
17	Oklahoma	2.00	33	Alabama	1.26	50	California	0.22

In relation to population, the smaller states are some of the most aggressive promoters of tourism. California and Florida are in the bottom ten states in per capita travel spending.

The report concludes that the primary role tourism offices see for legislatures is providing money. It includes comparative tables on state taxes earmarked for tourism development. But there are also recommendations for legislators on other topics, such as making sure travel efforts are coordinated with economic development and carried out pursuant to a plan.

FEDERAL-STATE RELATIONS

Federal Tax Burdens: The Tax Foundation (470 L'Enfant Plaza, S.W., Washington, DC 20024) has released its FY 1991 estimates of the per capita burdens of federal taxes, shown on Table 9.

Table 9: Estimated Per Capita Burden Of Federal Taxes, FY 1991

Rank	State	Amount	Rank	State	Amount	Rank	State	Amount
1	Connecticut	\$6,801	18	Minnesota	\$4,265	34	North Carolina	\$3,503
2	New Jersey	6,314		United States	4,235	35	Tennessee	3,464
3	Massachusetts	5,487	19	Florida	4,177	36	Arizona	3,446
4	Alaska	5,442	20	Ohio	4,008	37	Oklahoma	3,236
5	New York	5,285	21	Colorado	3,985	38	North Dakota	3,221
6	Maryland	5,116	22	Wisconsin	3,972	39	Montana	3,221
7	Delaware	5,085	23	Vermont	3,906	40	Kentucky	3,099
8	New Hampshire	4,921	24	Kansas	3,895	41	South Dakota	3,078
9	Illinois	4,816	25	Missouri	3,850	42	Alabama	3,066
10	Nevada	4,709	26	Oregon	3,800	43	Idaho	3,010
11	California	4,670	27	Indiana	3,724	44	South Carolina	2,994
12	Rhode Island	4,576	28	Texas	3,697	45	Louisiana	2,970
13	Virginia	4,387	29	Nebraska	3,669	46	Arkansas	2,924
14	Michigan	4,356	30	Georgia	3,669	47	New Mexico	2,915
15	Hawaii	4,304	31	Iowa	3,646	48	Utah	2,800
16	Pennsylvania	4,294	32	Maine	3,646	49	West Virginia	2,782
17	Washington	4,265	33	Wyoming	3,623	50	Mississippi	2,456

The size of the numbers is the most noticeable feature of the calculation, with the average family of three paying nearly \$13,000 in federal taxes. The burden continues to grow, with the Foundation estimating the per capita burden will rise 6% to nearly \$4,500 in FY 1992. Because the primary federal tax base is personal income, the distribution among states closely mirrors per capita income comparisons. Because statistics are available by state on federal spending by category, it is possible to calculate "terms of trade" with the federal government. For example, statistics showing major gainers (e.g., New York) and losers (e.g., California) from federal grants and the taxes that pay for them appear in States In Profile (Table F-2).

Federal Grant Increases: It has become increasingly difficult to blame the federal government for spending cutbacks that have caused fiscal problems for state government. Federal aid has been growing faster than inflation for some years. In the President's FY 1992 budget, grants to state and local government are slated to increase by 7.8%, well above the percentage increase likely in what state and local governments raise from their own taxpayers. Former NCSL fiscal expert Steven Gold recently gave a speech titled: "Is The Federal Government Responsible For State Fiscal Problems?" He concluded:

The major sources of state fiscal problems are the rapid growth in spending on Medicaid, prisons, and elementary-secondary education, accompanied by inadequate growth of revenue. The federal government is partly responsible for state fiscal problems because Medicaid is a federal program, because it has allowed the recession to

occur, and because of its tax policy and aid reductions. But the federal government is not primarily responsible for growth in prison or school spending, and the inadequacies of state tax systems would be causing revenue problems even if there were no recession. The federal government can be blamed for many problems, but the sad state of state finances is not one of them.

From the perspective of cities and counties, the picture is different. The major growth in federal aid has been in programs directed to states, like Medicaid, while the major attempted reductions have been in programs directed at local government, such as community and economic development. The trend is likely to continue as shown on Table 10.

Table 10: Proposed FY 1992 Grant Outlays In President's Budget

Program/Category	Amount (\$ billion)		Increase Over FY 1991
	FY 1991	FY 1992	
Medicaid	\$51.6	\$59.8	16.1%
Education and Social Services	26.8	27.6	3.0
Family Support (AFDC)	14.1	15.1	7.1
Subsidized Housing	10.3	11.6	13.5
Subtotal, Four Grant Categories	102.8	114.2	11.2
All Other Grant Programs	55.8	56.7	1.6
Total, All Programs	158.6	171.0	7.8

The table shows essentially all the growth in federal aid in a few programs. Two of the most rapid growing ones, Medicaid and AFDC, don't mean fiscal relief -- they simply reflect federal costs growing in lockstep with rising state costs. One, subsidized housing, primarily reflects commitments under old housing subsidy contracts. Finally, most cities and counties don't benefit substantially from the education and social services category. So while grant totals grow, city and county officials complain that federal aid is being reduced.

Federal Preemption And Mandates: Proposals for federal preemption of state laws continue to appear with regularity in the Congress. In health care, there is another substantial crop of proposed Medicaid mandates. Also, the administration's budget reflects the setting aside of a special fund of nearly \$1 billion associated with hospital reimbursements in Medicare and Medicaid. The winners would be hospitals in states that enact stipulated tort reforms, such as limits on non-economic damages in medical malpractice actions and elimination of joint and several liability. Losers would be hospitals (and thus patients and those paying their bills) in states that don't enact the legislation. Some states are already losing highway safety

money because they haven't complied with all the federal requirements for state law changes affecting driving under the influence.

California has decided it would rather fight than switch in response to the new federal nursing home guidelines. The decision to reject the standards was reflected in state legislative action last year and was affirmed by Governor Wilson who has written the President that the federal government was "improperly attempting to mandate standards on the states." State officials claim that the new requirements would cost about \$500 million a year, of which half would be state funds. California's problems are presumably shared in other states, with several other states said not to be in compliance either.

The federal remedy is to cut Medicaid funding, which federal officials are apparently reluctant to do. To date, they have announced withholding about \$24 billion out of about \$5 billion for the federal contribution to the California program. Federal officials recently announced that over 100 of the about 140 federal nursing home inspectors will be sent into the state.

There is litigation over the dispute in several courts. Compromise negotiations produced a mid-March preliminary agreement which defers action on the litigation, triggers more discussion on guidelines, and meanwhile treats guidelines as "tools" for inspectors rather than requirements.

MISCELLANY

Indian Reservations: For those states affected, the recent unanimous U.S. Supreme Court decision in Oklahoma Tax Commission v. Potawatomi Indian Tribe is an important affirmation of state government's ability to tax and to protect taxpaying merchants against other merchants paying no tax. The conclusion, reversing a lower federal court, is that Oklahoma can apply its cigarette tax to sales to non-Indians made on reservation land.

Litigation And State Finances: The latest U.S. Supreme Court opinion affecting state finances represents another potential cost to states, though it will have no immediate effect. The immediate issue is whether a Reconstruction Era civil rights statute, which already is now applied to such issues as suits against law enforcement agencies, can be used by an Ohio trucker in a tax dispute with Nebraska -- in addition to the other remedies available. By a 7-2 decision in Dennis v. Higgins, the court sided with the trucker.

TECHNICAL NOTES

Fiscal Situation: For extensive discussion of a "structural deficit" in California, see Legislative Analyst (925 L St., Sacramento, CA 95814), The 1991-92 Budget: Perspectives And Issues and California Taxpayers' Association (921 11th St., Sacramento, CA 95814), California's Budget Dilemma: Cyclical And Structural Problems in the organization's Cal-Tax News.

Economic Development: The state-by-state figures from Site Selection also cover the 1988-1990 period, which the magazine prefers for its comparisons. In addition to the new manufacturing facilities there are also statistics on expansions and on non-manufacturing facilities such as distribution centers for retailers and new communications facilities. By including new facilities outside manufacturing, somewhat different results can be produced. Those facilities, such as communications centers and warehouses, tend to be located in population centers.

The Louisiana dispute over considering environmental impacts in renewing tax exemptions is assessed in detail in the New York Times (2/27).

State And Local Governments: In New England and a few other situations (e.g., Maryland, New York City, Virginia), the general purpose local governments are responsible for the financing of schools. While these states separate school aid from unrestricted aid, the purchasing power is essentially fungible in practice. This makes trends to increase state school aid and decrease aid to cities and counties contradictory in those states. Because of the adverse fiscal circumstances, these states have been resolving the contradiction by cutting their support of local budgets.

State aid to local governments is measured by the Census Bureau and by a new publication of the National Association of State Budget Officers (444 North Capitol St., NW, Washington, DC 20001), State Aid To Local Government, 1990 which is the basis of the statistics in the article. NASBO, unlike the Census Bureau, excludes federal money passed through states to local government. The California proposal is assessed in 29-page section of the California Legislative Analyst's The 1991-92 Budget: Perspectives And Issues.

Federal Impacts: Gold is Director, Center for the Study of the States, State University of New York at Albany. His February 6 speech was to a local chapter of the American Society for Public Administration. The federal aid calculations were developed from Federal Funds Information for States' Special Analysis: Budget Of The United States Government: FY 1992.